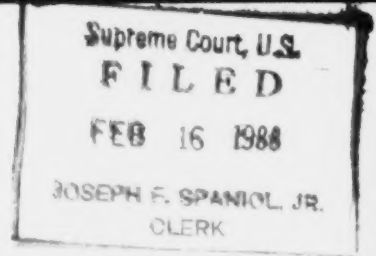


87-1308



No. 87-

IN THE
Supreme Court of the United States

OCTOBER TERM, 1987

TRASATLANTIC FINANCIAL CO., S.A., NAYARIT
INVESTMENTS, S.A., and FINVEST UNDERWRITERS
AND DEALERS CORP.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

**PETITION FOR WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT**

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QUESTIONS PRESENTED

1. Does the "misappropriation" of non-public information from a prospective bidder for the stock of a target corporation and the subsequent use of the information to acquire securities of the target corporation violate SEC Rule 10b-5?

2. Assuming that the answer is affirmative, may the SEC in an action to enjoin the violator obtain as ancillary equitable relief "disgorgement" of the profits from the securities transaction if the proceeds of the "disgorgement" are not to be used for "restitution" to victims of the fraud?

3. May "disgorgement" be used as a *quasi* penalty to deter wrongdoers by rendering their activities unprofitable?

4. May the proceeds of such disgorgement be used to create a fund to be disbursed in the uncontrolled and unreviewable discretion of the trial court, either to the U.S. Treasury or to other objects of the trial court's bounty?

PARTIES

The parties to the proceeding below were petitioners Trasatlantic Financial Co., S.A., Nayarit Investments, S.A., and Finvest Underwriters and Dealers Corp. The appeal of the defendant Giuseppe B. Tome was dismissed by the court below.

The other appellants Paolo Mario Leati and Lombardfin S.p.A. filed a separate petition for writ of certiorari.

The corporate petitioners have no parent companies, subsidiaries, or affiliates to list.

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TRASATLANTIC FINANCIAL CO., S.A., NAYARIT
INVESTMENTS, S.A., and FINVEST UNDERWRITERS
AND DEALERS CORP.,

Petitioners.

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

**PETITION FOR WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT**

Petitioners respectfully request that writ of certiorari issue to review a decision of the United States Court of Appeals for the Second Circuit, entered on November 24, 1987, which affirmed judgment against petitioners finding them to have committed securities fraud, enjoining them to desist from such frauds in the future, and ordering them to "disgorge" profits derived from the transactions in question, together with prejudgment interest.

OPINIONS BELOW

The opinion of the Court of Appeals (per Lumbard, J.) is reported as *SEC v. Tome*, 833 F.2d 1086 (2d Cir. 1987) and is reprinted in the appendix to this petition, *infra*, at A-1-21.¹ The decision of the United States District Court for the Southern District of New York and two supplements thereto (per Pollack, J.) are reported as *SEC v. Tome*, 638 F. Supp. 596, 629 and 638, respectively, (S.D.N.Y. 1986), and are reprinted in the Appendix to this petition, *infra* at A-25-82, A-83-96, and A-97-100.

JURISDICTION

The decision of the United States Court of Appeals for the Second Circuit, for which review is sought, was entered on November 20, 1987. That decision affirmed the judgment of the United States District Court of the Southern District of New York, entered on July 22, 1986, after trial to the Court, enjoining petitioners from violating the anti-fraud provisions of the securities laws and ordering them to disgorge profits connected with a past violation. This Court has jurisdiction to review the judgment of the Court of Appeals under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

Title 15, United States Code

§ 78j. Manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange —

* * *

¹ Citations to the Appendix to this petition are denoted by "A" followed by the page number ("A-—"). Citations to the joint exhibits as submitted to the Court of Appeals are designated as "JE" followed by the page number ("JE-—"). Citations to the joint appendix as submitted to the Court of Appeals are designated as "JA" followed by the page number ("JA-—").

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

17 Code of Federal Regulation

§ 240.10b-5 Employment of manipulative and deceptive devices.

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

- (a) To employ any device, scheme, or artifice to defraud,
 - (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
 - (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
- in connection with the purchase or sale of any security.

STATEMENT OF THE CASE

The facts are set forth in the opinion of the Court of Appeals (A-4-12) and in that of the District Court (A-26-58). They concern events surrounding a hostile tender offer by Joseph E. Seagram & Co. ("Seagram") for St. Joe Minerals Corporation ("St. Joe").

Petitioners' liability is predicated on the actions of Giuseppe B. Tome, who had power of attorney over their bank accounts at a Swiss bank and used it to trade for them in St. Joe stock and options.

Tome, a citizen of Italy and resident of Switzerland, was a financial expert who enjoyed an international reputation as an investment adviser and expert in foreign currencies. On meeting Tome, Edgar E. Bronfman, the chairman and chief executive officer of Seagram, was impressed by Tome's expertise in financial matters, and a close friendship developed between them. The genesis of the "fiduciary" relation of Tome to Seagram is to be found in that friendship. Bronfman was the sole possible source of Tome's "inside" information about Seagram's takeover plans (JE-158).

It was common knowledge that, in the latter part of 1980, Seagram had about 5 billion dollars available for acquisitions and was looking for suitable targets (A-6).

During a hunting trip in the middle of December, 1980, Bronfman discussed with Tome a plan for Seagram to acquire Santa Fe. Bronfman had come to consider Tome as a sort of general European consultant, and he wanted Tome's opinion as to how such an acquisition would be viewed by the European investment community. The discussion was not limited to Santa Fe, but also included other companies which, like Santa Fe, were rich in coal and other natural resources. Bronfman *might* even have mentioned Seagram's short list of potential acquisition candidates—Santa Fe, Amax, and St. Joe (A-6).

At the beginning of February, 1981, Bronfman informed Tome that Seagram had decided not to proceed with the acquisition of Santa Fe. Shortly thereafter Seagram also dropped Amax from the list of possible acquisitions, but Bronfman could not remember whether he mentioned this to Tome. However, on March 6, 1981, SoCal made a publicized tender offer for Amax so that Tome, at least at that date, knew that Amax was no longer available as an acquisition target for Seagram (A-39).

The District Court reasoned that from all that Tome was told he could deduce that St. Joe was Seagram's only remaining viable takeover target (A-39, n. 22).

On March 9, 1981, Tome called Bronfman to invite him for dinner for the following evening. Bronfman declined on the

ground that he had to leave for Montreal on the next day to attend a meeting of the board of Seagram. Despite sharply conflicting evidence, the District Court concluded that Tome could deduce that at the board meeting it would be decided that Seagram should make a tender offer for St. Joe and that action by Seagram was imminent. The day after the telephone conversation with Bronfman, March 10, Tome bought for the petitioners call options on St. Joe stock and the stock itself (A-41).

On the following morning, March 11, Seagram announced its bid for St. Joe, and St. Joe's stock price soared (A-10).

ARGUMENT

I.

THE "MISAPPROPRIATION" OF INFORMATION FROM A TENDERING CORPORATION AND ITS USE TO TRADE IN SECURITIES OF THE TARGET CORPORATION DOES NOT VIOLATE RULE 10b-5 SINCE THE "MISAPPROPRIATOR" HAS NO FIDUCIARY RELATIONSHIP TO THE TARGET CORPORATION OR ITS STOCKHOLDERS.

Petitioners' liability is predicated on the conclusion that "Tome traded [on their behalf] on material nonpublic information *in breach of his fiduciary duties to Seagram* in violation of Rule 10b-5" (A-21).² (*Italics supplied*). The conclusion embodies the finding that Tome had "misappropriated" confidential information from the tendering corporation (Seagram) and used it to trade in the target corporation's (St. Joe's) securities.

The validity of the "misappropriation theory" of liability for securities law violations was last before this Court in *Carpenter v. United States*, 108 S. Ct. 316 (1987), but it remained unresolved

² The Court of Appeals at one point (A-4) mistakenly states that the District Court had found that petitioners had also violated §14(e) of the Securities Exchange Act, 15 U.S.C. §78n(e) (1981), and Rule 14e-3. However, the District Court expressly rejected as unnecessary the application of §14(e) (A-71). The Court of Appeals later corrected the mistake (A-21).

because the Court was evenly divided. The very fact that this Court considered the issue betokens its importance. Unless it is resolved, the validity of every SEC action based on this theory is in doubt. Now that the full membership of the Court has been restored, it is appropriate and important that this issue be finally settled.

The "misappropriation theory" of liability for securities law violations was first enunciated in *Chiarella v. United States*, 445 U.S. 222 (1980). A printer's employee had misused confidential information about an impending tender offer to buy securities of the target corporation. This Court reversed his conviction for violating SEC Rule 10b-5 since he was not in a fiduciary relation to the target or its stockholders. Absent such a relationship, the failure to disclose the information does not constitute fraud.

The Government contended that Chiarella had defrauded his employer by sullyng the employer's reputation for probity and as one to whom confidential information could safely be entrusted. The subsequent use of the fraudulently obtained information to buy securities of the target corporation made the fraud one "in connection with the purchase or sale of [a] security" as denounced by SEC Rule 10b-5, despite the fact the employer, and not the seller of the securities, was the victim of the fraud.

Although several justices favored the Government's theory, since it had not been submitted to jury, this Court left for another day the answer to the question posed by the Government's arguments. *Chiarella*, 445 U.S. at 235-37.

The prevailing opinion, however, seemed to adopt the common sense notion that the general purpose of the securities laws was to protect investors and not the reputation of financial printers *cf. Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975). To apply the misappropriation theory and thus create a new species of fraud under Section 10(b) would "depart [] radically from the established doctrine that [the] duty [to disclose] arises from a specific relationship between two parties. . . [and] should not be undertaken absent some explicit evidence of congressional intent." *Chiarella*, 445 U.S. at 233;

quoted with approval and adopted in *Moss v. Morgan Stanley Inc.*, 719 F.2d 5, 16 (2d Cir. 1983), *cert denied sub nom.*, *Moss v. Newman*, 465 U.S. 1025 (1984).

The view that the misappropriation theory is not well founded is also held by the principal draftsman of Rule 10b-5. See, Freeman, *The Insider Trading Sanctions Bill — A Neglected Opportunity*, 4 Pace L. Rev. 221 (1984).

Drawing an implausible distinction between *Moss*, a private action for damages on the one hand, and criminal prosecutions and SEC actions on the other, the Second Circuit adopted the misappropriation theory as applied to an employee of an investment bank in *United States v. Newman*, 664 F.2d 12 (2d Cir. 1981), *aff'd after remand*, 722 F.2d 729 (2d Cir.), *cert. denied*, 464 U.S. 863 (1983); as applied to a printer's employee in *SEC v. Materia*, 745 F.2d 197 (2d Cir. 1984), *cert. denied*, 471 U.S. 1053 (1985); and finally as applied to a newspaper writer in *United States v. Carpenter*, 791 F.2d 1024 (2d Cir. 1986), *aff'd*, as to mail fraud, and by an equally divided Court as to securities fraud. 108 S. Ct. 316 (1987).

It is not without significance that the District Court in reaching its conclusion in the case at bar relied on the Circuit Court's decision in *Carpenter* (A-62), and on the clearly mistaken assumption that all nine of the then members of this Court supported the misappropriation theory (A-64).

Carpenter, in any event, makes plain that it is unnecessary to distort the securities laws in order to deal adequately with the predicate fraud, even if only intangible interests are involved. Such fraud can be dealt with conventionally, e.g., as mail or wire fraud. There seems to be little to gain by bringing it within the purview of the securities laws. But even in this respect, the case at bar breaks new ground. In all cases dealing with the misappropriation theory, there was at least reputational injury to the victim. Here, however, the misappropriation was incapable of causing Seagram any reputational or other injury, for Seagram itself was free to buy stock of its target. Nor is there any suggestion anywhere in the case that Seagram was injured.

It would seem that Tome's conduct here falls even below the threshold of cognizable injuries to intangible interests.

The failure of *Carpenter* to resolve the question of the validity of the misappropriation theory of insider trading (because the Court was equally divided) leaves the law as uncertain as if a split among circuits had occurred. Such a split is not likely to occur, for it is well known that litigation involving the securities laws is concentrated primarily in the Southern District of New York, so that circuits other than the Second rarely have occasion to deal with problems arising out of such litigation.

Even prior to the *Carpenter* decision by this Court, the uncertainty as to what constitutes unlawful insider trading was recognized as a problem in urgent need of solution. To this end, Sen. Riegle introduced a bill (S. 1380) intended to remove uncertainties. The bill was the product of a distinguished panel of securities law experts, and, as Sen. Riegle stated in introducing it, it reflected their concerns, among them the concern whether "the misappropriation theory [was] an appropriate basis for insider trading liability[.]" and "what breaches of duty would render a defendant liable[.]" He noted that uncertainties surrounding these questions "divert energy into developing convoluted legal theories[.]" Prophetically, Senator Riegle added: "There is little prospect that the problems in the law will be resolved judicially any time soon." 133 Cong. Rec. S 8246 (daily ed. June 17, 1987).

Recent press comments have also urged the desirability of ending the uncertainty in this field.³

The pending legislation, even if passed in the near future, could not end the quagmire that presently engulfs litigation

³ N.Y. Times, Aug. 10, 1987, at D-1; Washington Post, Nov. 12, 1987, at E-1.

After this Court failed to settle the validity of the misappropriation theory in *Carpenter*, a commentator wrote: "[The unsettled] state of law has led to inventive theories from prosecutors and defendants' lawyers and non-stop litigation seeking to define the contours of the wrong." The result has been a field day for lawyers to litigate and a quagmire for lawyers to provide counsel. Smith (former SEC Commissioner), "Can Insider Trading Be Defined?", N.Y.L.J., Dec. 3, 1987, at 1.

involving the misappropriation theory, nor could it retroactively deal with cases to be brought in the future concerning events predating the possible passage of remedial legislation. It is common knowledge that the recent volume of mergers and acquisitions has given rise to a flood of litigation in this field. The SEC announced that it means to add to the flood.⁴

It would seem desirable for the efficient administration of justice that the question which evenly divided this Court in *Carpenter* be resolved in the context of this case.

II.

EQUITY COURTS LACK JURISDICTION TO ORDER DISGORGEMENT IN THE ABSENCE OF CLAIMANTS ENTITLED TO RESTITUTION UNDER SUBSTANTIVE LAW

Assuming, *arguendo*, that a violation of the securities laws can be predicated on the misappropriation theory, it would permit the SEC to seek injunctions against future violations pursuant to §21(d) of the Securities and Exchange Act of 1934, 15 U.S.C. §78u(d) (1981). It does not follow, indeed it is plain error and in conflict with applicable decisions of this Court, that disgorgement of profits may be ordered as an ancillary remedy.

The misuse of the disgorgement remedy for purposes other than restitution has created, and will create in the future, vast funds to which there are no legitimate claimants. The disbursement of these funds evidently is relegated wholly to the unprecedented, uncontrolled, and uncontrollable discretion of district courts. As pointed out in Point IV *infra*, the creation of such funds is a recent innovation without precedent or analogy and cannot be fitted into accepted legal categories. It departs so far from the accepted and usual course of judicial proceedings as to call for the exercise of this Court's power of supervision.

⁴ N.Y. Times, Jan. 7, 1988, at D-1, Jan. 14, 1988, at D-11, Jan. 18, 1988, at D-1.

The misappropriation theory is based on the assumption that the victim of the fraud is the entity from which the confidential information has been misappropriated. Rarely, however, has the victim suffered any real loss. On the other hand, the traders to whom the misappropriated information has not been revealed, are not entitled to damages. *Moss v. Morgan Stanley Inc.*, 719 F.2d 5 (2d Cir. 1983), *cert. denied sub nom. Moss v. Newman*, 465 U.S. 1025 (1984) (based on *Chiarella v. United States*, 445 U.S. 22 (1980)).

The Circuit Court holds that it is not material to the "equitable" power of the District Court to grant "disgorgement," whether private parties have been damaged by the purported wrong (A-24).

The square holding of this Court to the contrary in *Tull v. United States*, 107 S. Ct. 1831 (1987), is sloughed off in a footnote on the untenable ground that it did not deal with securities law violations (A-24).

In *Tull*, the Government contended that a civil penalty measured by profits was "similar to an action for disgorgement of improper profits, traditionally considered an equitable remedy. . ." *Id.* at 1839. This Court, rejecting the argument, held:

An action for disgorgement of improper profits is, however, a poor analogy. Such an action is a remedy only for restitution. . . . Restitution is limited to "restoring the status quo and ordering the return of that which rightfully belongs to the purchaser or tenant." *Porter v. Warner Holding Co.*, 328 U.S. 395, 402, 66 S.Ct. 1086, 1091, 90 L.Ed. 1332 (1946).

107 S. Ct. at 1839.

Similarly, in *Curtis v. Loether*, 415 U.S. 189 (1974), this Court rejected equity jurisdiction to order disgorgement, because ". . . there [was no] sense in which the award here can be viewed as requiring the defendant to disgorge funds wrongfully withheld from the plaintiff." *Id.* at 197. Clearly, the decision of the Circuit is not only in conflict with *Tull*, but also with all other pertinent decisions of this Court.

Essentially, disgorgement is no more than a synonym for restitution. *SEC v. Flight Transportation Corp.* 699 F.2d 943, 945 n. 2 (8th Cir. 1983).

The quotation (A-23-24) from the decision in *SEC v. Commonwealth Chemical Securities, Inc.*, 574 F.2d 90, 102 (2d Cir. 1978), is inappropriate and torn out of context so as to distort its meaning. Judge Friendly at that point was merely discussing the special measure of damages which applies to restitution. Restitution cases are governed by the rule that if "a tort results in the unjust enrichment of the defendant at the plaintiff's expense, the plaintiff may . . . sue . . . [for] restitution of the benefits which the defendant has so received." *Prosser and Keeton on Torts* (5th ed. 1984) §94, at 672-73. In this respect restitution differs from the tort basis of recovery which is measured by the plaintiff's loss. *Id.* p. 675.

The true meaning of *Commonwealth* is to be gathered from its holdings:

While from the standpoint of a defendant in an action for violation of the securities laws there may be no great difference between paying money in response to a private suit for damages and in a SEC action for injunction and disgorgement *wherein the SEC makes the proceeds of disgorgement available to injured parties*, the suit by the SEC is decidedly more analogous to the traditional jurisdiction of equity to award restitution.

574 F.2d at 96 (emphasis supplied).

To order disgorgement in cases in which there are no legitimate claimants entitled to restitution runs counter not only to the decisions of this Court but also to the settled course of equity jurisprudence which knows only "restitution" as an equitable remedy. It leads to the irrational result that the funds "disgorged" may be distributed according to the uncontrolled discretion of the trial court. For absurd suggestions for distribution which have been made, see below, Point IV.

III.

DISGORGEMENT MAY NOT BE USED AS A QUASI-PENALTY SOLELY TO DETER WRONGDOERS BY RENDERING THEIR ACTIVITIES UNPROFITABLE

The District Court justifies disgorgement in this case on the ground that it is *the most effective means to deter* violations of the securities laws by making such activities unprofitable (A-79). The Court of Appeals evidently accepts this justification (A-24). Deterrence, however, is properly the function of punitive measures, and Congress has provided ample criminal sanctions for violations of the securities laws or other species of fraud. Nor is it necessary to transgress the fixed boundaries of equity jurisdiction to deprive violators of their profits. The Insider Trading Sanctions Act of 1984, Pub. L. No. 98-376, 98 Stat. 1264 (1984), in pertinent part, 15 U.S.C. §78u(d)(2)(A), provides that the SEC in appropriate cases may seek a civil penalty up to three times the profit gained as a result of such unlawful conduct. But such penalties are beyond the reach of equity, for they must be tried to a jury. *Atlas Roofing Co. v. Occupational Safety & Health Review Commission*, 430 U.S. 442 (1977).

In a different context *United States v. Parkinson*, 240 F.2d 918, 922 (9th Cir. 1956), held "Anything which savors of a penalty should not be permitted unless Congress has expressly so provided, since *the spirit of equity abhorred such punitive measures.*" (emphasis supplied).

In earlier cases the Second Circuit stringently applied the limits on remedies available in equity. In the seminal case dealing with true insider trading, *SEC v. Texas Gulf Sulphur Co.*, 446 F.2d 1301 (2d Cir.), *cert. denied*, 404 U.S. 1005 (1971), the Court clearly announced that the equitable remedy of disgorgement is available only where the object of that relief is remedial and not "punitive." *Id.* at 1307-08.

Similarly, in *SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1104-05 (2d Cir. 1972), the Court reversed that portion of the District Court's order which required defendants to disgorge profits and income earned on the proceeds of their

fraud. The Court found such an order to be "a prohibited penalty to the extent that it would exceed the damages to which defrauded investors were entitled."

In holding for the first time that the disgorgement remedy was available in securities cases, *Texas Gulf* relied on two precedents in this Court. Both clearly permit the remedy to be used solely for restitution. In *Mitchell v. Robert DeMario Jewelry, Inc.*, 361 U.S. 288 (1960), this Court rejected the argument that an order to reimburse, lost wages would be punitive, stating that "...the public remedy is not thereby rendered punitive, where the measure of reimbursement is *compensatory* only." 361 U.S. at 293 (emphasis supplied). To the same effect is *Porter v. Warner Holding Co.*, 328 U.S. 395, 402 (1946).

IV.

THE PROCEEDS OF DISGORGEMENT MAY NOT BE USED TO CREATE FUNDS TO BE DISPOSED IN THE UNCONTROLLED AND UNREVIEWABLE DISCRETION OF THE TRIAL COURT TO OBJECTS OF THE TRIAL COURT'S BOUNTY

In this and many other cases, funds were ordered paid into court while no persons had claims against the funds under substantive law either for restitution or otherwise. As a consequence, no one has standing to object to proposed distributions or to ask for appellate review of proposed distributions. The disposition of the funds is literally left to the uncontrolled and unreviewable discretion of trial courts — an unprecedented innovation. Large funds await such distribution, and it would seem imperative to clarify their status.

The final judgment of the District Court in this case merely provides that the sums to be disgorged are to be paid into the registry of the District Court, distribution to be made subject to further order of the Court (JA-882-3). The Court of Appeals deems it irrelevant whether private parties have been damaged by the "fraud" (A-24).

Actually it is plain that no one could have a legitimate claim to restitution. The sellers of the target's securities have no claim. See, *supra*, p. 7. Assuming *arguendo* that Seagram suffered some injury, it may have an action at law for damages, but what was taken from it cannot be restored, which defeats the possible application of the "restitution" remedy. See, *supra*, pp. 10-11.

The problem of how to dispose of disgorged funds, which are a new species of *res nullus*, first arose in *SEC v. Materia*, Fed. Sec. L. Rep. (CCH) [1983-1984 Transfer Binder] ¶99,583, at 97, 287 (S.D.N.Y. 1983), *aff'd*, 745 F.2d 197 (2d Cir. 1984), *cert. denied*, 471 U.S. 1053 (1985). The Court of Appeals did not pass on the question as to how such a fund is to be distributed. It held that whether a defendant has breached a duty to a particular plaintiff "is germane only in the context of private civil litigation." 745 F.2d at 202. Evidently the Court held that equitable jurisdiction expands if a governmental agency is the plaintiff.

—The District Court, however, dealt with the problem at length. Fed. Se. L. Rep. (CCH) [1983-84 Transfer Binder] ¶99,583, at 97,287. The Court reserved decision over the ultimate disposition of the fund pending appellate finality of its judgment. While the Court left open the opportunity for the defrauded employer-printer or the target company to prove damages, the Court doubted that anyone in fact was damaged. It indicated that probably the fund would be paid to the U.S. Treasury. In effect, it would be treated as a penalty for unlawful conduct. It requires no argument that such treatment is improper. Penalties may not be imposed except after a trial to a jury. *Supra*, p. 12.

SEC v. Blavin, 760 F.2d 706 (6th Cir. 1985), on which the Court of Appeals relies (A-24), deals with funds that remain after all legitimate claims have been satisfied. *Blavin* invents a power of equity "to confiscate" such wrongful profits. It attributes the failure to realize that equity has such power to "the misguided belief that disgorgement is a form of restitution." *Id.* at 713.

The belief is certainly not "misguided." It incorporates settled law as recently reiterated by this Court. See, *supra*, p. 10. In

oral argument before this Court in *Carpenter*, the Solicitor General agreed that disgorgement can merely provide for restitution or restoration of the *status quo* and that the beneficiary of restitution could only be the victim, in *Carpenter*, *The Wall Street Journal*. The Solicitor General also agreed that the amount to be restored must be equivalent to what the victim had been deprived of. Freeman, *Disposing of Fraud Funds: Issues Remain Unresolved*, N.Y.L.J., Dec. 7, 1987, p. 33-4. Applying this view to this case, since Seagram, the victim, suffered no damage at all, there would be no occasion for any "restitution."

Freeman also points out the magnitude of the problem posed by funds paid into court to be distributed at the court's discretion. In *Carpenter* alone, over \$600,000 remain undistributed; in *SEC v. Boesky*, No. 86 Civ. 8767 (S.D.N.Y. Nov. 14, 1986), \$50,000,000 is involved; in *SEC v. Levine*, No. 86 Civ. 3726 (S.D.N.Y. June 14, 1986), several million dollars remain to be distributed. These millions were paid into court pursuant to consent orders, so there can hardly be any limit on the discretion of the court as to whom to distribute that portion of the funds not used for restitution. If the judgment in the case at bar were collected in full, over \$7,000,000 would be left to be distributed at the court's discretion. No legal norms exist which could restrain the absolute discretion of district courts in distributing these funds.

Freeman cites some of the suggestions which have been made as to how the funds should be distributed, among them, suggestions that the money should be paid to charities, to universities, to the corporations involved, to the "little guys" (whatever that might mean), or to the government.

The SEC has filed a proposal that the monies held in *Levine* be used to pay Mr. Levine's taxes and the remainder be given to groups called "investors." Such a distribution would obviously run counter to *Moss*, except presumably distributions to those victims which are not barred by *Moss*, *supra*, p. 7.

There are no legal norms for distributing funds to which no claimant is entitled under substantive law. The fact that disgorgement for purposes other than restitution leads to such

unprecedented and irrational problems is by itself a strong indication that disgorgement cannot be used in this manner. It has created a legal no man's land in which the imagination and even the whim of district courts, with the non-binding aid of the SEC, is given full play. It seems to call for an exercise of this Court's power of supervision.

CONCLUSION

For the foregoing reasons, petitioners respectfully pray that the Court issue writ of certiorari to review the judgments of the Court of Appeals for the Second Circuit.

Dated: February 10, 1988

Respectfully submitted,

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APPENDIX



UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 1098, 1099—August Term 1986

Argued: April 10, 1987 Decided: November 20, 1987

Docket Nos. 86-6192(L), 86-6194, 86-6196

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellee,

—against—

GIUSEPPE B. TOME, PAOLO MARIO LEATI, LOMBARD-
FIN S.p.A., TRASATLANTIC FINANCIAL CO., S.A.,
NAYARIT INVESTMENTS, S.A., FINVEST UNDERWRIT-
ERS AND DEALERS CORP., CERTAIN PURCHASERS OF
THE COMMON STOCK AND CALL OPTIONS FOR THE
COMMON STOCK OF ST. JOE MINERALS CORP., and
BANCA DELLA SVIZZERA ITALIANA,

Defendants,

PAOLO MARIO LEATI, LOMBARDFIN S.p.A., TRAS-
ATLANTIC FINANCIAL CO., S.A., NAYARIT INVEST-
MENTS, S.A., and FINVEST UNDERWRITERS AND
DEALERS,

Defendants-Appellants.

B e f o r e :

LUMBARD, OAKES, and CARDAMONE,
Circuit Judges.



Two appeals from a judgment entered in the Southern District by Judge Milton Pollack, holding appellants liable for violations of section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and Rule 10b-5 promulgated thereunder and directing disgorgement of profits from their insider trading.

Affirmed.



RICHARD A. KIRBY, Assistant General Counsel, Securities and Exchange Commission, Washington, D.C. (Paul Gonson, Solicitor, Daniel L. Goelzer, General Counsel, Jacob H. Stillman, Associate General Counsel, Thomas L. Riesenbergl, Special Counsel, Martha H. McNeely, Katharine B. Gresham, Randall W. Quinn, Attorneys, Securities and Exchange Commission, Washington, D.C., of counsel), *for Plaintiff-Appellee.*

PAUL J. BSCHORR, New York, N.Y. (White & Case, New York, N.Y., Robert M. Kelly, Dorothea W. Regal, Loreto Ruzzo, Bar-

bara Shea, of counsel), *for Defendants-Appellants Lombardfin S.p.A. and Paolo Mario Leati.*

BRUNO SCHACHNER, New York, N.Y., *for Defendants-Appellants Nayarit Investments, S.A., Trasatlantic Financial Co., S.A., Finvest Underwriters and Dealers Corp.*



LUMBARD, *Circuit Judge:*

On March 10, 1981, one day before Joseph E. Seagram & Co. ("Seagram") announced a hostile tender offer for St. Joe Minerals Corporation ("St. Joe"), Giuseppe B. Tome and his associates ordered massive purchases of St. Joe securities. Less than three weeks later, the SEC filed this suit originally charging Banca Della Svizzera Italiana ("BSI"), Irving Trust Company and "certain purchasers of call options for the common stock of St. Joe Minerals Corporation" with violations of the anti-fraud provisions of the federal securities laws. The complaint was amended on several occasions and ultimately named Tome, three Panamanian corporations in which he owned a beneficial interest (Trasatlantic Financial Co., S.A., Nayarit Investments, S.A., and Finvest Underwriters and Dealers Corp. (collectively the "Panamanian corporations" or "Panamanian defendants")), the "certain purchasers", Paolo Mario Leati, Lombardfin, S.p.A. and BSI as defendants.

After a bench trial on October 23, 1985, in the Southern District of New York, Judge Milton Pollack found

that the defendants had violated sections 10(b) and 14(e) of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78j(b), 78n(e) and Rules 10b-5 and 14e-3. *SEC v. Tome*, 638 F. Supp. 596 (S.D.N.Y. 1986). By a judgment entered on July 22, 1986, Judge Pollack enjoined the defendants from violating the antifraud provisions of the federal securities laws and ordered them to disgorge over \$2.7 million in profits obtained through trading on non-public information (plus over \$1.3 million in prejudgment interest). The Panamanian corporations¹ and Leati and Lombardfin appeal from that judgment.

Leati and Lombardfin claim that the district court lacked personal jurisdiction over them because of defects in the service of process. The Panamanian corporations join them in making three additional arguments: (1) they challenge the admissibility of the deposition testimony of Dionisio G. Csopey; (2) they attack the sufficiency of the evidence; and (3) they contend that the district court improperly ordered disgorgement of their profits. We affirm.

We summarize the salient facts, more fully recorded in the district court's opinion. The case of the Securities and Exchange Commission focused on Giuseppe B. Tome, an Italian national now residing in Switzerland. Tome began working as a registered representative in the securities industry at the Milan office of Bache & Co. in 1959. He moved to E.F. Hutton & Company, Inc. where he eventually became president of E.F. Hutton, International,

¹ On November 25, 1986, we granted the SEC's motion to dismiss Tome's appeal because he was, and still is, a "fugitive from justice," but denied the same motion as to the Panamanian defendants. We deny the SEC's request to reconsider the denial of its motion to dismiss the appeal of the Panamanian defendants.

S.A., and a director of E.F. Hutton & Company, Inc. In 1979, Tome resigned from Hutton and formed his own investment company, Compagnie Pour le Financement et l'Investissement, S.A. (Finvest Geneva) in Geneva, Switzerland. Tome is also a beneficial owner of the defendant Panamanian corporations. In March 1981, when the illegal transactions took place, he enjoyed discretionary power over their accounts at BSI, a Swiss bank based in Lugano, Switzerland.

Paolo Mario Leati is a sales representative and Lombardfin is a broker/dealer both of whom are registered with the SEC. In 1974, Leati, an Italian national living in Italy, and Dionisio G. Csopey left Merrill Lynch, Pierce, Fenner & Smith, Inc. and formed Lombardfin, S.p.A., a holding company whose subsidiaries and affiliates engage in securities and currency brokerage. Leati—the majority shareholder of and primary decisionmaker for Lombardfin—wielded discretionary authority over many of his clients' accounts. Finvest Geneva and Lombardfin, and consequently Tome and Leati, enjoyed a close working relationship evinced by office rental agreements, brokerage contacts, and other business arrangements.

In July, 1980, Tome met Edgar M. Bronfman, Chairman of the Board and Chief Executive Officer of Seagram, when the two flew on the Seagram company plane to a rodeo in Cheyenne, Wyoming. Tome subsequently developed a business relationship with Bronfman and in October, 1980, Tome, acting for Finvest Geneva, agreed to provide Seagram with information and advice about foreign currencies. In the same month, Finvest Geneva agreed to invest and manage ten million dollars for Seagram in various currencies, bonds and notes. Bronf-

man also opened a personal account at Finvest Geneva, over which he gave Tome discretionary authority.

In August, 1980, Seagram sold its interest in Texas Pacific Oil Company for \$2.3 billion. With this cash reserve and a \$3 billion line of credit, Seagram began looking for an acquisition candidate. Because of Bronfman's interest in coal as a primary energy source, Seagram focused on companies with significant coal assets, particularly Santa Fe Industries, Amax, St. Joe, and Union Pacific. In late 1980, Tome requested and received from Seagram a briefing on its policies, operations, and financials.

In making acquisition decisions, Bronfman "consider(ed Tome) sort of a European consultant to Seagram generally," 638 F. Supp. at 603, and looked to him for insight into how the European investment community would view an acquisition by Seagram. "Tome seized and actively solicited and nurtured this confidentiality, frequently probing into the internal reasons for Seagram's actions, asking Bronfman 'why?' " 638 F. Supp. at 603. In mid-December, 1980, Bronfman informed Tome that Seagram was looking "very hard" at Santa Fe and sought Tome's advice on the proposed acquisition. This conversation indicated to Judge Pollack that "Tome was looked upon and treated by Bronfman as an insider of Seagram, as he had become." *Id.* at 604. Tome probed why Seagram was interested in Santa Fe and when Bronfman expected to act. Bronfman testified that he and Tome "didn't just discuss Santa Fe, but companies like Santa Fe," and that he might even have mentioned Seagram's short list of potential acquisition candidates—Santa Fe, Amax, and St. Joe.

On January 13, 1981, the board of Seagram's parent corporation authorized Seagram to invest up to \$150 million in the stock of four companies, without being informed that the companies were Santa Fe, Amax, St. Joe, and Kimberly Clark. On January 28, Seagram decided not to proceed with the acquisition of Santa Fe. Bronfman conveyed this information to Tome by February 6, at the latest. In early February, Seagram also dropped Amax from the potential acquisition list. Bronfman could not remember whether he informed Tome that Amax had been removed from Seagram's acquisition list. According to Bronfman, "[a]lmost by a process of elimination, that left St. Joe." By February 25, 1981, Bronfman had decided to make a tender offer for St. Joe.

The price and volume of St. Joe securities trading remained relatively stable during February and March. Moreover, two weeks prior to Seagram's tender offer, Salomon Brothers & Co., a highly respected New York broker-dealer, executed sales of a large block of St. Joe stock on behalf of an institutional client. Apparently, Seagram's intentions were a well-kept secret.

Bronfman and Tome continued to see each other socially: They participated in a "joint venture" as investors in the Broadway musical "Sophisticated Ladies;" Bronfman, Tome and their wives spent vacations together in France, Virginia, and Mexico; and they talked frequently by telephone. On March 9, 1981, Tome called Bronfman in New York and invited him to dinner the following evening. Bronfman declined Tome's dinner invitation, stating that he would be in Montreal for a directors' meeting.

The next morning, March 10, 1981, Tome feverishly placed orders for St. Joe securities. Through BSI, Tome

purchased 1,055 options² on St. Joe common stock on behalf of the Panamanian corporations. Tome bought an additional 3,000 shares of St. Joe stock through Finvest Geneva on behalf of Finvest Underwriters and Dealers Corp. Tome later sold 2,000 of these shares, reaping an overnight profit of \$34,000 and exchanged the other 1,000 shares of St. Joe stock for 1,200 shares of Fluor Corporation. The trading profits were deposited in BSI's account at Irving Trust. On the morning of March 11, Seagram's public announcement of the tender offer foiled Tome's efforts to place orders for an additional 2,055 call options.

Tome also made numerous phone calls on March 10 to individuals at various foreign financial institutions urging them to purchase St. Joe securities. After telephone calls from Tome, Banque de Rone, a Swiss bank in Geneva, purchased 200 St. Joe shares and 50 St. Joe call options; Cramer, a Swiss bank client, bought 100 St. Joe call options and 1,000 St. Joe shares; and Compagnie de Banque et d'Investissements, another Swiss bank client, placed orders for 150 St. Joe call options and 1,100 shares. On the same day, Banque Gutzwiller and Trade Development Bank (TDB), both clients of Tome, bought 2,000 and 13,000 St. Joe shares respectively. Although Gutzwiller and TDB never received phone calls from Tome, the district court concluded that "Tome conveyed the inside information that he possessed to Gutzwiller and to TDB, and that they subsequently traded and profited personally on that information." 638 F. Supp. at 610.

² Each option gives the purchaser the right to buy 100 shares of the underlying stock on terms provided in the option.

Tome also called Leati in Milan on March 10. Two minutes after hanging up, Leati exercised his discretionary authority over his clients' accounts and began purchasing St. Joe securities. Before March 10, Lombardfin had never purchased or sold a single share of St. Joe. By the end of the day, Lombardfin had purchased 40,200 shares of St. Joe common stock and 500 St. Joe call options, which it subsequently liquidated for a net profit of \$1,345,925.

According to Leati, Tome said only "I'd buy [St. Joe]" when he telephoned. However, Leati's partner, Dioniso Csopey, told a different story, which the district court credited. Csopey testified that on March 10, Leati mentioned that he had learned from Tome that Seagram would make a tender offer for St. Joe in a few days. Leati agreed to pay Tome \$200,000 for this information, if a takeover in fact took place. Leati believed that Tome's claims "could well be true" because of Tome's close personal relationship to Seagram. With Csopey's assent, Leati placed additional orders for St. Joe securities on March 11, which were never executed because of the announcement of the tender offer. The next day Leati told the board of directors of Lombardfin of his agreement with Tome, admitted that Lombardfin had committed securities violations, but downplayed the risk of being caught.

Altogether, Tome and his confederates purchased call options on 185,500 shares of St. Joe stock, one-third of all such options traded at the Philadelphia Stock Exchange on March 10. The bulk of the options bought by Tome expired 11 days after they were purchased. They also bought at least 60,500 shares of St. Joe common,

representing 10.67% of the total volume in St. Joe stock sold on the New York Stock Exchange on March 10.

At 7:00 p.m. on March 10, the board of directors of Seagram's parent company held a special meeting. The meeting had been scheduled for the following day, but it was changed because of activity in St. Joe stock. At that meeting, the parent company authorized Seagram to make a tender offer for St. Joe. At 9:22 a.m. the following morning, March 11, Seagram announced publicly its bid for St. Joe and its stock price soared.

In New York on the evening of March 11, Bronfman, Tome and their wives went to see "Sophisticated Ladies". Although they discussed Seagram's tender offer, Tome said nothing about his trading the previous day. That night Bronfman gave a dinner party for twenty people in Tome's honor. Again, the two discussed the tender offer and again Tome failed to mention his dealings in St. Joe securities. On March 12, Tome liquidated his St. Joe holdings and instructed his clients to do the same.

On March 13, the SEC publicly announced an inquiry into possible insider trading on the Seagram offer for St. Joe stock. Tome left New York and returned to Switzerland on March 14. The following day, Tome called BSI and asked them to rearrange the option purchases to make it appear that Finvest Underwriters had not purchased any St. Joe options. BSI refused.

The SEC commenced suit on Friday, March 27, 1981. The complaint named BSI and Irving Trust Company of New York, where the proceeds of BSI's trading in St. Joe had been deposited, as nominal defendants. The remaining defendants were identified by category as "certain

purchasers" of St. Joe call options. The district court ordered frozen BSI's account at Irving.³

The following Monday, March 30, Bronfman learned about the SEC investigation of alleged insider trading in St. Joe securities originating in Switzerland; he immediately phoned Tome. According to Bronfman, Tome was "the only person I knew in Switzerland that would have any knowledge one way or another of anything that was going on." At about 7:20 that night, Tome returned his call and denied any wrongdoing, but admitted that the matter was "a little more complicated than that." He promised to elucidate when he saw Bronfman in New York the following week.

On Monday, April 6, Tome visited Bronfman at his New York apartment. Tome acknowledged that one of his people had placed an order for 3,000 shares of St. Joe stock but claimed that he had not been personally involved. When Bronfman asked point blank, "Were those shares in any way beneficially owned by you or members of your family?" Tome responded, "No." Tome repeated his story the following morning in Bronfman's office, with Bronfman's attorney present. Judge Pollack noted that later "Tome's counsel conceded on the record that Tome had a beneficial interest in St. Joe stock purchases." 638 F.2d at 613 (footnote omitted).

Tome left the United States soon thereafter, missing a business meeting on April 9. He has not returned to the

³ On November 18, 1986, BSI satisfied the district court's judgment, which ordered it to pay into the registry of the court \$2 million—most of the Panamanian corporations' illegal profits plus interest. BSI has not appealed from that judgment and the Panamanian defendants lack standing to appeal in BSI's stead.

United States since 1981, and has refused to appear in this action or related criminal proceedings.

I. SERVICE OF PROCESS

Leati and Lombardfin contend that the district court did not have personal jurisdiction over them because they never received valid service of process. When the SEC instituted this suit on March 27, 1981, it was aware only that a substantial number of the March 10th trades in St. Joe securities had been conducted through BSI. Swiss bank secrecy laws prevented the SEC from ascertaining the identities of the individual purchasers involved. Therefore, the original complaint named only BSI, Irving Trust (where BSI had deposited the proceeds of the trades) and "Certain Purchasers of Call Options for the Common Stock of St. Joe Minerals Corporation" as defendants. These purchasers were defined in the complaint as "certain persons, the identities and addresses of whom are unknown to the plaintiff at this time." On November 12, 1981, BSI, facing contempt sanctions, informed the SEC that Tome and the Panamanian defendants had ordered purchases of St. Joe securities during the period in question. The SEC amended the complaint on December 14, 1981 to include Tome and the Panamanian corporations as defendants.

During its subsequent investigation of Tome's involvement, the SEC learned that on March 10, 1981, Tome had telephoned several foreign financial institutions, including Lombardfin, and that these institutions had purchased St. Joe securities immediately after these telephone conversations took place. Leati submitted an

affidavit to the SEC⁴ taken in Milan dated April 28, 1982, in which he admitted that he purchased St. Joe securities on March 10, 1981 through Lombardfin but denied knowingly trading on nonpublic information. He also submitted his records of those trades to the SEC. The Lombardfin trading records indicated that the St. Joe transactions were "unsolicited"—in other words, that the trades were executed without use of Leati's discretionary authority over the accounts. Unbeknownst to the SEC at that time, the information contained in the Leati affidavit and the Lombardfin records was false.

The SEC filed a second amended complaint on May 13, 1982, which expanded the category of "certain purchasers" to include persons, whose identities were unknown to the SEC and who had effected transactions in St. Joe securities through a number of foreign banks and securities dealers, including Lombardfin. At this point the SEC had no evidence suggesting that Leati and Lombardfin had knowingly participated in illegal trades, therefore, they were not named as defendants in the second amended complaint.

The record reflects the many difficulties that the SEC experienced in attempting to serve process on Tome and the Panamanian defendants. Due to these difficulties and because the identities of the other purchasers remained unknown despite diligent efforts, the SEC sought an order pursuant to Fed. R. Civ. P. 4(i)(1)(E) (which allows service on a foreign defendant "as directed by order of the court") authorizing service on all defendants by publication of the complaint and summons in the *International Herald Tribune* and *La Suisse*. Judge Pollack granted the

⁴ The record does not show the circumstances under which the affidavit was submitted.

motion by order on May 13, 1982. The *International Herald Tribune* is an English language paper which is widely read by the international financial community in Europe; *La Suisse* is a French language paper circulated in and around Geneva. When it was discovered that publishing the complaint and summons in *La Suisse* would violate Swiss law, the order was amended and the complaint and summons were published in all editions of the *International Herald Tribune* for four successive weeks.

On September 4, 1985, the SEC deposed Dionisio Csopey, Leati's former partner, pursuant to a subpoena in New York. Csopey's deposition testimony revealed that the affidavit and trading records submitted by Leati to the SEC were misleading. According to Csopey, when Tome called Leati on March 10, he told Leati that "Seagrams would make, in the next few days, make a tender offer for St. Joe Minerals." 638 F. Supp. at 615. Leati told Csopey that Tome was passing this information on to Lombardfin in exchange for \$200,000, if the tender offer in fact occurred. Csopey also testified that during a Lombardfin board of directors' meeting on March 11, 1981, Leati explained the circumstances surrounding the St. Joe transactions and admitted that the firm had committed securities violations by trading on inside information. However, he "downplayed the risk of being caught by remarking that Lombardfin S.p.A. had accounted for only a 'small fraction' of the previous day's total trading volume." *Id.* at 616.

During Letter Rogatory proceedings (authorized by the district court in September 1985) in Milan, Italy on October 2, 1985, Leati for the first time admitted that some of the trades he executed on March 10, 1981

involving St. Joe securities were not "unsolicited" and that Tome had told him to buy St. Joe. The testimony at the Letter Rogatory proceedings and the Csopey deposition testimony established that Leati was involved in the insider trading scheme with Tome. The SEC then sought to amend the second amended complaint to identify Leati and Lombardfin by name as among the group referred to as "certain purchasers" on the face of the complaint. This amendment made no changes in the allegations contained in the body of the complaint. On October 17, 1985, the district court issued an "Order to Show Cause Why Leave to Amend . . . Complaint in respect of the 'Purchasers' and to substitute therefor in part the names of . . . [Leati] and Lombardfin . . . should not be granted." The order required Leati and Lombardfin to show cause at the United States Courthouse at 10:00 a.m. on October 23rd, "or as soon thereafter as counsel can be heard." On October 18, a member of the Italian bar personally delivered the order on behalf of the SEC to Leati and Lombardfin at their office in Milan.⁵ At the commencement of the trial on October 23, 1985, Judge Pollack heard the SEC's motion to amend the complaint to identify Leati and Lombardfin as two of the "certain

⁵ Francesco Abbozzo handed envelopes containing the order to show cause, the affidavit in support of the order, and the memorandum in support of the application for the order and leave to amend the complaint to Leati at 12:45 p.m. on October 18 in Milan. The same documents were also delivered to Leati's and Lombardfin's attorney at 12:50 p.m. Several pages of the affidavit and memorandum were missing due to transatlantic transmission problems. Abbozzo informed Leati of the omissions and indicated that he would return with the missing pages. At approximately 4:45 p.m., Abbozzo delivered complete copies of the documents to a secretary at Lombardfin. Leati then emerged from an office and ejected him from the premises. Complete copies were also delivered to Leati's counsel the same day.

purchasers" named as defendants. Leati and Lombardfin elected not to appear at either the hearing or the trial. Judge Pollack found that the 1982 service by publication coupled with the evidence that Leati and Lombardfin "clearly were aware of the pendency of this litigation but chose not to participate in it" satisfied the notice and service requirements and concluded that because Leati and Lombardfin had already been charged as unknown defendants in 1982, substitution of their names on the complaint was not a substantive amendment requiring reservice of the complaint. On July 22, 1986, the district court entered judgment holding Leati and Lombardfin liable for violations of the anti-fraud provisions of the securities laws. Leati and Lombardfin now challenge the district court's jurisdiction. We reject their challenge.

To submit a party to the jurisdiction of a court, due process has long been held to require the giving of notice in such a manner that there can be little doubt that the party has actual notice of the claims in order to appear and defend. *Wuchter v. Pizzutti*, 276 U.S. 13, 24 (1928). Where the plaintiff can show that deliberate avoidance and obstruction by the defendants have made the giving of notice impossible, statutes and caselaw have allowed substitute notice by mail and by publication in media of general and wide circulation. Thus, as business dealings have become increasingly interstate and international, the means of giving notice have been extended to meet these situations, so that parties may be held accountable in our courts of justice.

Gradually we have come to permit and approve the giving of notice under a substitute system limited by the requirements of the due process clause. "An elementary and fundamental requirement of due process in any

proceeding which is to be accorded finality is notice reasonably calculated, under the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections." *Mullane v. Central Hanover Bank and Trust Co.*, 339 U.S. 306, 314 (1950). Publication of the complaint and summons in the *International Herald Tribune* was "reasonably calculated" to notify the unidentified purchasers of St. Joe options, including Leati and Lombardfin, of the suit against them. The SEC was aware that the illegal trades had been effected through several European financial institutions, yet its efforts to identify the guilty parties were thwarted by Swiss secrecy and other foreign laws. The SEC reasonably concluded that the purchasers resided or conducted business in Europe and chose a publication likely to be read by international investors. The propriety of this method of notice must also be considered in light of the fact that members of the securities industry like Leati and Lombardfin may be expected to be aware of a publicly announced SEC investigation involving insider trading during a high-visibility takeover. The facts here are distinguishable from cases where notice was published in a small regional paper or the advertisement contained nothing which would draw a party's attention to it. *E.g.*, *Mullane*, 339 U.S. at 315. Notice by publication, in the circumstances surrounding this action, was reasonably calculated to apprise the interested parties of the lawsuit.

The "reasonably calculated" analysis need not be relied on exclusively in this case because we are not dealing with the question of the adequacy of *constructive notice*. There can be no doubt that by October 23, 1985 when the matter was tried before Judge Pollack, Leati and Lom-

bardfin knew of the suit brought by the SEC and the claims against them.⁶ In fact, they were cognizant of the action years before the SEC discovered evidence of their involvement. As a registered representative, Leati realized on March 10, 1981 that he was committing a serious violation of the United States securities laws by trading on inside information. The next day he explained to the Lombardfin board of directors that the St. Joe trades were illegal, but downplayed the risk of being caught. Tome visited the Lombardfin offices regularly throughout 1981. During this time, he and Csopey had discussions about the size of the legal fees for all involved in this action. Leati told Csopey that Tome had pressed him "for contributions to the legal fees and to a pool which would settle the case." 638 F. Supp. at 616. Leati's submission to the SEC of a false affidavit of April 28, 1982 and misleading trading reports designed to obscure his involvement in the illegal transactions provide further evidence that he was fully aware that he was among those referred to as "certain purchasers" on the face of the complaint and that he understood the nature of the suit and the charges against him. Prior to obtaining the information from the Csopey deposition and the Letter Rogatory proceedings, the SEC sought the cooperation of Leati and Lombardfin to determine the circumstances of the trades and the persons involved. Leati and Lombardfin declined to cooperate and Lombardfin's legal counsel refused to accept service of an SEC investigative sub-

⁶ The SEC moved to supplement the record on appeal, or, in the alternative, to remand to the district court, in order to produce evidence that Leati and Lombardfin took notice of the complaint and summons published in the *International Herald Tribune*. In view of our finding that Leati and Lombardfin received proper notice, we deny the motion.

poena. Leati and Lombardfin also petitioned the Italian court in August of 1985 to set aside the district court's Letter Rogatory and refused to produce any documents thereby requested. On October 18, 1985, five days before trial was to begin, Leati was personally served with a copy of the order to show cause why he and Lombardfin should not be named as defendants in this case. With full knowledge of the pendency of the action against them, Leati and Lombardfin elected not to appear. They raise their objections for the first time in this appeal.

Leati and Lombardfin claim that because the SEC admittedly knew their names and addresses when notice was published in the *International Herald Tribune*, such service was invalid. *Mennonite Bd. of Missions v. Adams*, 462 U.S. 791, 800 (1983); *Mullane*, 339 U.S. at 320. Certainly, if a defendant's name and address are known or may be obtained with reasonable diligence, service by publication will not satisfy the requirements of due process. *Mennonite Bd. of Missions*, 462 U.S. at 800. However, this is not such a case. Although Leati and Lombardfin were well aware that they were among those named on the complaint as "certain purchasers" in this action, the SEC was not. Leati's affidavit and the misleading trading records deceived the Commission into believing that they were not involved in Tome's scheme. The SEC was unaware of the the nature of their involvement until September of 1985. Thus, at the time that Judge Pollack authorized service on the "purchasers" by publication, Leati and Lombardfin were "unknown defendants" whose identities could not have been ascertained with reasonable diligence by the SEC. *Id.* As the Supreme Court pointed out in *Mullane*, "in the case of persons missing or unknown, employment of an indirect

and even a probably futile means of notification is all that the situation permits and creates no constitutional bar to a final decree foreclosing their rights." *Mullane*, 339 U.S. at 317.

"The fundamental requisite of due process of law is the opportunity to be heard." *Grannis v. Ordean*, 234 U.S. 385, 394 (1914). This record clearly establishes that Leati and Lombardfin were afforded such an opportunity and that they made a conscious decision to ignore this action until after a judgment had been rendered against them.

II. ADMISSIBILITY OF CSOPEY'S TESTIMONY

All appellants challenge the admissibility of the deposition testimony of Dioniso G. Csopey, Leati's former partner at Lombardfin, which was introduced into evidence at trial in lieu of his appearance. The district court admitted Csopey's testimony, over objection, under the co-conspirator exception to the hearsay rule. Fed. R. Evid. 801(d)(2)(E). *SEC v. Tome*, 638 F. Supp. 629 (S.D.N.Y. 1986). The Panamanian defendants contend that the testimony is inadmissible because (1) there was no extrinsic proof of the existence of a conspiracy between Leati and Tome; (2) Leati's statements to Csopey were not made in furtherance of the conspiracy; and (3) there was no showing they were co-conspirators with Leati. We disagree.

First, there was ample evidence that Tome and Leati were co-conspirators. They had a close working relationship, and it was immediately after the phone call from Tome that Leati began placing large orders for St. Joe securities. Second, when Leati made the statement to Csopey, he was trying to convince Csopey to assist him in

making additional St. Joe purchases on March 11, 1981. *Id.* at 636. The district court could reasonably conclude that Leati made the statements "in furtherance" of the conspiracy. *See United States v. Rahme*, 813 F.2d 31, 35-36 (2d Cir. 1987). Third, because the Panamanians were Tome's alter egos, the district court properly treated them as co-conspirators.

There is no merit to Leati and Lombardfin's contention that Csopey's testimony was inadmissible against them because they were not given notice of his deposition. As discussed above, in September 1985 when Csopey's deposition was taken, Leati and Lombardfin were aware of the action and that they were among the category of purchasers named in the complaint. When they chose to ignore the action, they forfeited their right to attend Csopey's deposition and to object to its admission at trial. They may not make their objection for the first time on appeal. *See, e.g., United States v. Mangan*, 575 F.2d 32, 44 (2d Cir.), *cert. denied*, 439 U.S. 931 (1978). Csopey's deposition was taken under oath after notice was given to the named defendants. There is nothing in the record to suggest that Judge Pollack's decision to admit the testimony at trial was improper.

III. SUFFICIENCY OF THE EVIDENCE

Defendants' claims of insufficient evidence are without merit. The SEC introduced overwhelming evidence that Tome traded on material nonpublic information in breach of his fiduciary duties to Seagram in violation of Rule 10b-5. Through his confidential relationship with Bronfman and Seagram, Tome was privy to information not yet made public; one day prior to the announcement of the

takeover, and the morning after having a conversation with Bronfman, Tome began frantically trading in St. Joe securities and advised his clients and friends to do likewise; trading by Tome and his associates accounted for one-third of the activity in St. Joe call options on the Philadelphia Stock Exchange and 10% of the activity in St. Joe common stock on the New York Stock Exchange one day prior to the announcement of Seagram's tender offer; and Tome purchased one of the most speculative types of security available—call options due to expire in 11 days.

Finally, Tome went to great pains to cover-up his trading. He traded through BSI, a Swiss bank protected by Swiss secrecy laws, although he would have received a discount on brokerage fees had he dealt through Baird-Patrick & Co., Inc. where he was a registered representative. He repeatedly misled Bronfman about his activity in St. Joe securities, and he fled the United States soon after this action began. Thus, Judge Pollack's findings were amply supported by the record.

We also agree with Judge Pollack that the evidence showed that Leati and Lombardfin knew that nonpublic information had been divulged to them in breach of a fiduciary duty. *Dirks v. SEC*, 463 U.S. 646, 660 (1983). Csopey testified that Leati told him that he had agreed to pay Tome \$200,000 for information that Seagram was about to make a tender offer for St. Joe. Leati made the large purchases of St. Joe stock immediately after talking with Tome, indicating his belief in the reliability of Tome's information. He told Csopey that he believed that the information "could well be true" because of Tome's ties to Seagram. At a Lombardfin board meeting on March 11, Leati admitted that his trades in St. Joe

securities on the previous day had "obviously" been "a violation" of the United States securities laws. And, after the SEC commenced this action, Leati attempted to deceive the Commission by submitting a false affidavit with doctored trading records.

Leati and Lombardfin also complain that there was insufficient evidence to support an injunction against them. Judge Pollack found that there was a likelihood of recurrence because Leati had intentionally misappropriated inside information, had shown no remorse for doing so, had attempted to mislead the SEC, and because Leati had the opportunity to repeat his conduct in the future because of his position as a registered securities sales representative. We agree. There was "positive proof of a reasonable likelihood that past wrongdoing [would] recur" necessary for an injunction. *SEC v. Bausch & Lomb, Inc.*, 565 F.2d 8, 18 (2d Cir. 1977); see, e.g., *SEC v. American Board of Trade, Inc.*, 751 F.2d 529, 537-38 (2d Cir. 1984). An injunction also properly issued against Lombardfin which is dominated by Leati as its owner and manager.

IV. DISGORGEMENT

The appellants claim that the district court erred in ordering disgorgement of the proceeds of the illegal trades. They contend that the disgorgement remedy's only purpose is to provide restitution for victims of the illegality. In *SEC v. Commonwealth Chem. Sec., Inc.*, 574 F.2d 90 (2d Cir. 1978), Judge Friendly explained that "the primary purpose of disgorgement is not to compensate investors. Unlike damages, it is a method of forcing a defendant to give up the amount by which he was un-

justly enriched." *Id.* at 102.⁷ As the Sixth Circuit has recently stated in *SEC v. Blavin*, 760 F.2d 706, 713 (6th Cir. 1985) "[o]nce the Commission has established that a defendant has violated the securities laws, the district court possesses the equitable power to grant disgorgement without inquiring whether, or to what extent, identifiable private parties have been damaged by [the] fraud." *Id.* Whether or not any investors may be entitled to money damages is immaterial. The paramount purpose of enforcing the prohibition against insider trading by ordering disgorgement is to make sure that wrongdoers will not profit from their wrongdoing. Tome and his satellites must therefore "disgorge a sum of money equal to all the illegal payments [they] received." *Id.*

The judgment of the district court is affirmed.

⁷ We do not believe the Supreme Court's passing reference to the restitutionary nature of the disgorgement remedy in *Tull v. United States*, 107 S. Ct. 1831, 1839 (1987), was meant to cast doubt on the propriety of disgorgement in cases such as this. *Tull* dealt not with the power of a district court to order disgorgement in securities fraud actions, but with the right to a jury trial in an action seeking civil penalties and injunctive relief under the Clean Water Act. However, *Tull* answers the Panamanian defendants' argument that they had a right to a jury trial; the Seventh Amendment right to a jury trial does not apply to the equitable actions for disgorgement. *Id.*

SECURITIES AND EXCHANGE COMMISSION, Plaintiff,

v.

Giuseppe B. TOME, Paolo Mario Leati, Lombardfin S.p.A.,
Trasatlantic Financial Co., S.A., Nayarit Investments, S.A., Finvest
Underwriters and Dealers Corp., Certain Purchasers of the Com-
mon Stock and Call Options for the Common Stock of St. Joe
Minerals Corp., and Banca Della Svizzera Italiana, Defendants.

No. 81 Civ. 1836(MP).

United States District Court,
S.D. New York.

June 3, 1986.

As Amended July 15, 1986.

Ira Lee Sorkin, Regional Administrator, S.E.C. by Anne C.
Flannery, Robert B. Blackburn, Joseph G. Mari, Philip M. Gior-
dano, Jennifer M. Russell, for plaintiff,

John F.X. Peloso, Daniel B. McIntyre, Sage Gray Todd & Sims,
New York City, for defendant Giuseppe B. Tome.

Bruno Schachner, New York City, for defendants Transatlan-
tic Financial Co., S.A., Nayarit Investments, S.A., Finvest Under-
writers and Dealers Corp.

Chester J. Straub, David Trachtenberg, Willkie Farr &
Gallagher, New York City, for defendant Banca Della Svizzera
Italiana.

FINDINGS AND OPINION

MILTON POLLACK, Senior District Judge:

THE ACTION

This is a civil insider trading liability action, brought by the Securities and Exchange Commission ("SEC"), authorized by Section 21(d) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. § 78u(d), seeking an injunction and other ancillary relief, including disgorgement of ill-gotten gains, against defendants based on defendants' violations of the antifraud provisions of the securities laws and regulations. Subject-matter jurisdiction is posited on Sections 21(e) and 27 of the Exchange Act, 15 U.S.C. §§ 78u(e) and 78aa.

This action arises from the defendants' purchases of call options on the common stock of St. Joe Minerals Corporation ("St. Joe"), as well as of the stock itself, on March 10, 1981, the day immediately prior to the announcement by Joseph E. Seagram & Company of a hostile tender offer for all of the outstanding common stock of St. Joe. The issues were presented to the Court at a Bench trial.

The case reveals a crass abuse and betrayal of a personal and professional relationship of trust and confidence for personal gain. The principal defendant, Tome, exploited his confidential relationship with Seagram and with its Chairman of the Board and Chief Executive Officer, Edgar Bronfman, to obtain and misuse nonpublic information of Seagram's preparations to bid for control of St. Joe at \$45 per share of common stock. Acting a day ahead of the announcement of that bid, on March 10, 1981, Tome positioned himself and his tippees to garner millions of dollars in unlawful gains by purchasing vast quantities of call options on St. Joe stock, and the stock itself, which was trading at about \$30 per share, from unsuspecting sellers while Seagram was putting the finishing touches on the as-yet unannounced bid. Within days after the March 11th announcement of the hostile tender offer, which sent the St. Joe stock up to over \$45 per share and sky-rocketed the options accordingly, Tome and his tippees cashed

in on their St. Joe call options and common stock. Tome fraudulently concealed his misappropriation of this confidential corporate information and his breach of the confidential relationship from Bronfman and from Seagram, falsely denying that he had made any St. Joe purchases and falsely denying any participation in the market when confronted and questioned specifically by Bronfman. As his identity in the illegal conduct came to light through a prompt SEC investigation, Tome fled this country and has remained abroad since. His conduct, and that of his cohorts, was meticulously pieced together by the SEC, resulting in this suit.

I. BACKGROUND

A. *Identity and Interrelationship of Defendants*

Those involved in the misconduct complained of form an intricate international web which needs to be detailed in order to understand its ramifications.

1. *Tome*

Giuseppe B. Tome ("Tome") is an Italian national who resides in Switzerland.¹ He first became involved in the securities industry in 1959 as a Registered Representative in the Milan, Italy office of Bache & Co. ("Bache"). Through the years, Tome was promoted within the Bache organization, eventually becoming Chairman of Bache & Co. (Overseas) S.A., located in Geneva, Switzerland. Tome left Bache in 1973 for a position as Vice President of E.F. Hutton & Company, Inc. ("Hutton"). At Hutton, Tome was involved with their international division, eventually managing several hundred registered representatives located in twenty-two offices worldwide. When he resigned from Hutton

¹ Unless a contrary time period is indicated, all of the factual information stated in this Opinion, although expressed in the present tense, applies to the relevant time period involved here, the latter part of 1980 through April 1981. In addition, all hours, unless otherwise noted, refer to Eastern Standard Time.

on February 3, 1979, Tome was President of E.F. Hutton International, S.A., and was on the Board of Directors of Hutton.²

Sometime after leaving Hutton in 1979, Tome formed *Compagnie Pour le Financement et l'Investissement, S.A* ("Finvest Geneva"), a securities firm headquartered in Geneva, Switzerland, of which he is the President and Chief Executive Officer. Finvest Geneva is controlled by, and is part of, a larger holding company, *Infinvest Holdings, N.V.*, a Netherland Antilles corporation. See *infra* note 5.

In order to execute securities trades on the United States exchanges, Tome was also a registered representative from January 1980 until June 30, 1981, with Baird-Patrick & Co., Inc. ("Baird-Patrick"), a United States broker-dealer.³ Tome forwarded, and sometimes himself initiated, orders to buy or sell securities traded on U.S. exchanges, primarily the New York Stock Exchange, for the accounts of his clients, or for companies affiliated with Finvest Geneva, to Baird-Patrick for execution.

Tome regularly visited the United States for periods of time for business and social reasons; in early April 1981, however, he

² According to a former colleague and former close friend of Tome, Alain Cheneviere, whom Tome hired while at Bache and took with him when he moved to Hutton, Tome left Hutton suddenly, under contentious circumstances. When Tome left he asked Cheneviere to "almost quit immediately" and follow him to some then, as yet, vague new venture; Cheneviere refused and became quite upset when Tome told him, Tome's confidence, "a gigantic lie." Cheneviere is presently a Vice President of Hutton in its Geneva office.

³ Apparently Tome was less than fully candid with Mr. Patrick Chairman of Baird-Patrick, concerning Tome's activities other than those on behalf of Baird-Patrick. Patrick did not know Tome was associated in any way with Finvest Geneva, except as the Baird-Patrick registered representative for that account. In addition, Patrick did not know that Tome, in fact, regularly executed option trades through A.G. Becker, another U.S. broker-dealer and a competitor of Baird-Patrick. Patrick did not consider it permissible, given Tome's relationship with Baird-Patrick, for Tome to put through option trades for his customers with A.G. Becker directly.

left the United States abruptly,⁴ missing a scheduled business meeting on April 9, 1981. Tome was indicted in New York on August 7, 1984, charged with criminal violation of the securities laws. He has not been in the United States since 1981 and did not return to face the criminal charges. Although represented by counsel in this case, he refused to answer any interrogatories related to the transactions involved herein on the ground of the Fifth Amendment privilege against self-incrimination.

2. *Finvest Geneva*

Although not technically a defendant in this action, Finvest Geneva is discussed here next, both for purposes of clarity, and because of Tome's proprietary interest in and his use of Finvest Geneva in the matters involved herein.

Finvest Geneva belongs to a group of related enterprises (the "Finvest Group")⁵ that, through Tome's design, were represented to potential clients as engaging in securities and commodities brokering, in trading and underwriting, Eurobond transactions, currency management, portfolio management, as well as in investment banking.

Finvest Geneva itself was founded by Tome in 1979; Tome is its majority shareholder and two banks, Banque Privee and Compagnie de Banque et D'Investissement ("CBI"), are minority

⁴ The SEC instituted this suit on March 27, 1981. At that time, however, the SEC did not know exactly who was responsible for the St. Joe trades. But the SEC did wish to speak to Tome since he was the registered representative on the St. Joe stock trades occurring through Baird-Patrick (approximately 3,000 shares). Although Tome was aware that the SEC wanted to talk with him, he did not volunteer to see them but in fact left the country before they were able to track him down.

⁵ Ininvest Holdings, N.V., a Netherland Antilles corporation, owns 100% of Finvest Securities and Commodity Brokers Corp., 100% of defendant Finvest Underwriters and Dealers Corp. ("Finvest Panama"), and 32% of International Corporation for Financing and Investment in Mexico Ltd. Finvest Geneva is also controlled by, and is a part of, Ininvest Holdings, N.V. The 1981 Second Quarter Report to Ininvest Holdings shareholders was signed by Tome.

shareholders. Finvest Geneva's clients comprise Swiss banks, persons with accounts in Swiss banks, and depositors of Swiss banks. Finvest Geneva managed portfolios for approximately 25-30 clients. Finvest Geneva was run from day to day by Tome, and when he was not there, by either of two other employees, Mr. Del Pozzo or Mr. Bulletti.⁶

Finvest Geneva had discretionary authority over at least some of its clients' accounts. The only persons exercising discretion over clients' accounts, however, were Tome and, to a lesser extent, Del Pozzo and Bulletti.⁷ Thus, without the client's advance knowledge, Tome would often buy and sell stock and/or options for a particular clients' account.

3. *Lombardfin S.p.A.*

Lombardfin S.p.A.,⁸ a holding company for various subsidiaries and affiliates, engaged primarily in securities and currency brokering, was formed in 1974 by Paolo Mario Leati ("Leati") and Dionisio G. Csopey ("Csopey"). Lombardfin S.p.A. and Finvest Geneva had a close working relationship because of Leati's relationship with Tome. In fact, Lombardfin S.p.A.'s two principal foreign affiliates were renting their *only* office space from Finvest Geneva.⁹ Conversely, Tome often visited the Milan office

⁶ Del Pozzo was Tome's assistant for prospecting and for the Mexican ventures. Bulletti coordinated the operating and administrative side of Finvest Geneva.

⁷ According to Lawrence B. Franko, Professor of International Business Relations at The Fletcher School, Tufts University, who formerly was a consultant/employee of Finvest Geneva, "Mr. Tome essentially made the decisions [on currency management], and the people who executed the orders were executing his decisions."

⁸ In 1980-81, Lombardfin S.p.A.'s Board of Directors consisted of Riccardo Argenziano (chairman), Leati (vice-chairman), Mr. Spadacini, and Csopey. Its officers were Leati (general manager), Csopey (manager), and Mrs. Patricia Arbucias (secretary & manager).

⁹ In fact, according to Professor Franko, *see supra* note 7, Ms. Brax's "office" consisted merely of "an excess desk" and a telephone, with access to telex facilities.

(Footnote continued)

of Lombardfin S.p.A.'s domestic subsidiary and used its facilities (e.g., telephone, telex machine, quotation machine) to conduct his business. In addition, Lombardfin Securities Underwriters, a Lombardfin S.p.A. 100% owned affiliate, executed trades in the Eurobond market on Finvest Geneva's behalf because Finvest Geneva did not have the capacity to clear trades. Finvest Geneva had a securities trading account with Lombardfin Securities Underwriters, Ltd., which was opened on or about September 28, 1979.

4. *Leati and Csopey*

Leati is an Italian national residing in Italy. In 1974, he and Csopey left their employment at Merrill Lynch, Pierce, Fenner & Smith, and formed Lombardfin S.p.A., as a joint stock company. In 1980-81, Leati was the majority shareholder (60-75%) in Lombardfin S.p.A. Csopey (12.5%) and Fiduciaria di Investimenti, a company, were the minority shareholders. Csopey was not named as a defendant in this action.

Leati was the decision-maker for Lombardfin S.p.A. and its subsidiaries. He had discretion over accounts of many Lombardfin S.p.A. clients and thus could, and often did, trade shares and/or options for a client's account without that client's advance knowledge or specific approval.

5. *BSI*

Banca Della Svizzera Italiana ("BSI") is a Swiss banking institution with principal offices in Lugano, Switzerland. It maintains securities trading accounts for customers. It acted for Tome's interests and the accounts of the so-called Panamanian defendants, i.e., NICO, TFCO, and Finvest Panama, discussed next.

6. *NICO*

To acquire the St. Joe securities he purchased directly on March 10, 1981, Tome used the brokerage trading accounts maintained at

Thus, this Lombardfin-Finvest Geneva relationship consisted of much more interaction than that of a mere sublessor-sublessee relationship.

BSI for three Panamanian entities in which Tome had a beneficial interest, namely NICO, TFCO, and Finvest Panama.

The first of these BSI accounts, Nayarit Investments, S.A. ("NICO"), is a Panamanian company which was formed on or about May 31, 1978. NICO's principal line of business is the management and administration of assets deposited in bank accounts. Tome provided NICO with investment advisory and management services, for which no fees were paid to Tome. Tome was a beneficial owner of and held discretionary authority and a power of attorney over the NICO account.

7. TFCO

The second of these trading accounts at BSI, Trasatlantic Financial Co., S.A. ("TFCO"), is a Panamanian company which was formed on or about March 25, 1980. TFCO's principal line of business is the management and administration of assets deposited in bank accounts. Here again, Tome provided TFCO with investment and advisory services, without fee. Tome was a beneficial owner of the TFCO account and held discretionary power over it.¹⁰

8. Finvest Panama

The third of the trading accounts at BSI, Finvest Underwriters and Dealers Corp. ("Finvest Panama"), is a Panamanian corporation that was formed on or about June 26, 1979. Tome has been a beneficial owner of the Finvest Panama account with BSI and has had discretionary power over it. *See supra* note 10.

As noted previously, *see supra* note 5, Finvest Panama is a wholly owned subsidiary of Ininvest Holdings, N.V. (*i.e.*, the Finvest Group), and thus is directly related to Finvest Geneva, and thus to Tome.

¹⁰ On March 15, 1981, after purchasing the St. Joe stock and options that form the subject of this action, Tome called Claudio Nesã, assistant manager of defendant BSI, and asked him to reallocate the option purchases from Finvest Panama to NICO and TFCO. Tome stated that the reason he was doing this was "to secure greater confidentiality within *his organization*." (emphasis added).

B. *The Confidential Relationship*

At the base of this suit, we find a personal acquaintance that flowered and bloomed into an intimate friendship and a professional association in which trust and confidence were reposed in Tome, of which he callously took shoddy and unlawful advantage.

Edgar M. Bronfman ("Bronfman") is the Chairman of the Board and Chief Executive Officer of Joseph E. Seagram & Co. ("Seagram"), an Indiana corporation, and of its parent corporation, Seagram Company Ltd., a Canadian corporation.

Bronfman met Tome in July 1980 when they flew together, as part of a group of fourteen people, on the Seagram Company airplane to Cheyenne, Wyoming to attend a rodeo. Bronfman's wife had met Tome and his wife earlier that month. The Tomes promptly ingratiated themselves, resulting in an invitation to accompany the Bronfmans on the trip to help Mrs. Bronfman celebrate her birthday.

Using his opportunity on the airplane, Tome turned to financial matters and discussed currencies with Bronfman. Using a reprint of an article written about him that he happened to have handy, Tome showed Bronfman his oft-repeated "insight" that any American corporation keeping all its accounts in U.S. dollars is thereby "going short" on other currencies.

Within weeks of this enticing initial discussion, Bronfman introduced Tome to Harold Fieldsteel, Seagram's chief financial officer. In a memorandum to Fieldsteel, dated August 5, 1980, immediately prior to a meeting between Tome and Seagram's officers on the topic of Seagram's currency position, Bronfman stated that Tome's "record warrants our taking a serious look at his firm's [*i.e.*, Fininvest Geneva's] capabilities," and that Bronfman was "not at all interested in any defensive attitude on [Seagram's] part."

After the initial associations, Tome moved in on the Bronfmans and intensified the social relationship and his business approach.

In October 1980, through Tome's efforts, Finvest Geneva obtained as a major client Seagram with which it signed two agreements. On October 2, 1980, Tome, acting for Finvest Geneva, signed a "Foreign Exchange Advisory Agreement" with Seagram under which, in exchange for \$100,000 annually (later reduced to \$50,000), Finvest Geneva agreed to provide Seagram with information and advice regarding world currencies and to form for it a foreign exchange advisory committee, the members of which were to be selected by Finvest Geneva with Seagram's approval. On October 8, 1980, Tome, acting for Finvest Geneva, entered into an "Investment Management Agreement" with Seagram under which Finvest Geneva was given discretion to invest ten million dollars of Seagram's money in various currencies, bonds and notes, and to exchange it from one currency to another. As a management fee, Finvest Geneva would receive one-eighth of 1%, per quarter, of the average amount of funds held in the Seagram account.

Although not memorialized as a "formal" relationship, but clearly indicated by subsequent conduct, Bronfman, in his own words, "consider[ed Tome] sort of a European consultant to Seagram generally." It was in the context of the actual relationship that Bronfman conveyed to Tome a stream of material non-public information concerning Seagram's acquisition plans. Tome seized and actively solicited and nurtured this confidentiality, frequently probing into the internal reasons for Seagram's actions, asking Bronfman "why?" Bronfman, on the other hand, states that he sought Tome's insight into "how the European investment community would look at Seagram if [it] made such an acquisition." Unquestionably, Tome was Bronfman's friend and advisor, had formal contractual relationships with Seagram, through Finvest Geneva, and had vast experience in the securities industry;¹¹ clearly, Tome was looked upon and treated by Bronfman as an insider of Seagram, as he had become.

¹¹ Apparently, Tome was not as open with his other associates, to whom he only selectively revealed his activities and experience and only when it behooved him to do so. For example, although Bronfman knew that Tome was the principal

(footnote continued)

In his personal finances as well, Bronfman trusted and confided in Tome. Bronfman opened a personal account with Finvest Geneva for trading in commodity futures and currencies; he gave Tome a power of attorney and discretion over his personal account. Bronfman consulted with Tome "as an advisor [for] general business purposes." This advisory function led to a "joint venture" between Bronfman and Tome, on behalf of NICO, as investors in the Broadway musical "Sophisticated Ladies." In fact, Bronfman even replaced with his own money a \$5,000 bounced check that Tome issued to the "Sophisticated Ladies" partnership on behalf of NICO. On another occasion, Tome suggested a "joint venture" to Bronfman whereby they would buy a block of stock in the Bache securities firm.

Underlying and encouraging these confidential and business relationships, both Seagram-related and personal, between Bronfman and Tome were a pervasive series of social contacts. After initially meeting Tome on the plane trip for Bronfman's wife's birthday, Bronfman saw Tome regularly, approximately a dozen times, until April 1981 and exchanged telephone calls from time to time.

Given the brief period of time they had known each other, Bronfman's and Tome's close social contacts were extensive and significant, giving Tome the access to Bronfman and thus to Seagram that he promoted. In November 1980, Bronfman, his wife, and another couple spent a weekend with Tome in Mageve, France at Tome's ski lodge. On that same trip, Bronfman and his wife were personal guests at Tome's house in Geneva, Switzerland, at a dinner party. In December 1980, Tome visited Bronfman and his wife during hunting season at their home in Charlottesville, Virginia. Bronfman and his wife spent the Christmas and New Year's holidays in 1980-81 with Tome and his wife on a boat off Mexico.

officer of Finvest Geneva and knew that he was affiliated with the U.S. securities firm of Baird-Patrick, the head of Baird-Patrick, the one who hired Tome, did not even know that Tome had any relationship with Finvest Geneva except as Baird-Patrick's registered agent for its Finvest Geneva account.

C. Seagram's Acquisition Plans

In August 1980, just after Bronfman met Tome, Seagram sold its interest in Texas Pacific Oil Company for \$2.3 billion dollars. With this tremendous cash reserve, Seagram began looking at companies for purposes of finding an acquisition candidate. Seagram set up an acquisition committee, lined up a \$3 billion dollar line of credit (that was available after November 1980),¹² and hired Arthur D. Little & Company to do a macro study of how the world would change in the next twenty to thirty years, and thus where the best business opportunities lay. Bronfman was "fascinated" with coal as the primary source of energy after oil in the next 20-30 years and began to look at companies that had coal assets, particularly Santa Fe, Amax, St. Joe, and Union Pacific.¹³

In late 1980, Tome requested that Seagram provide him with a general briefing on its policies, operations, and financials, and he informed Seagram's officers that he was interested in discussing with them Seagram's use of the proceeds it had obtained from the Texas Pacific Oil sale. The data was provided to him, and Bronfman spoke with Tome as a consultant to Seagram about its acquisition and hostile tender offer plans.

Sometime during the Fall of 1980, Seagram considered purchasing up to twenty percent of the outstanding shares of Texaco.¹⁴ Bronfman testified that Seagram "proceeded and got pretty

¹² Tome knew of this line of credit before it was generally reported to the public. By letter dated November 25, 1980, Tome indicated his awareness of Seagram's preparation for a "jumbo" borrowing of money. That Seagram was making preparation for a large borrowing was reported in the *Wall Street Journal* on December 12, 1980.

¹³ Union Pacific, though, was almost immediately ruled out by Bronfman because "it's just a little too large to even contemplate [acquiring]."

¹⁴ Promptly Texaco became the most heavily traded stock by Finvest Geneva in November and December 1980, according to Mr. Andrea Manzoni, former employee of Finvest Geneva who placed orders for securities purchases as either Tome, Del Pozzo, or Bulletti instructed him.

close to actually making a tender" for Texaco. Around December 10, 1980, Bronfman decided that Seagram would not proceed with the Texaco tender.¹⁵

Immediately after deciding not to proceed with the Texaco stock purchase, Bronfman (and his investment bankers and acquisition committee) "started to focus on Santa Fe Industries." In mid-December, while Tome visited Bronfman at his house in Charlottesville, Virginia during hunting season, Bronfman discussed Seagram's acquisition plans with Tome in an attempt to determine "how the European investment community would look at Seagram if [it] made such an acquisition":

And he [Tome] asked, you know, had we gotten any closer to making any decision as to what we [Seagram] were going to do [about an acquisition] and I [Bronfman] said, yes I think we are looking very hard at Santa Fe. And we discussed it in general. *He wanted to know why.* I told him about the kind of asset play that it represented. (emphasis added).

Tome probed further, asking Bronfman "*when* do you think?" (emphasis added). Bronfman told him that it might take another couple of months, and that the investment banking firms of Goldman, Sachs, and Lazard Freres were advising Seagram on the matter.

Tome and Bronfman "didn't just discuss Santa Fe, but companies like Santa Fe."¹⁶ The coal resource

¹⁵ Finvest Geneva began selling Texaco stock and options beginning December, really developing around December 11, through the next several months, according to Mr. Federico Pignatelli, former employee of Finvest Geneva who placed orders for securities as he was instructed by either Tome, Del Pozzo, or Bulletti.

¹⁶ Finvest Geneva began buying Santa Fe stock heavily in late December 1980 and early January 1981, according to Manzoni. Except perhaps for Texaco, Santa Fe was the most heavily traded stock at Finvest Geneva during this time period.

companies that Bronfman had on his short list at the time were Santa Fe, Amaz, and St. Joe.¹⁷

During this mid-December conversation, Bronfman did not consider it necessary to caution Tome that the information Bronfman was giving him was confidential because:

I [Bronfman] didn't think it was necessary.... [because of Tome's] 20 years in this business. He ought to know the rules. I assume he does know the rules.... [The rules are] [t]hat basically [what I told him] was inside information[;] ... [y]es[, materially non-public information].

At a Board meeting of Seagram's parent corporation, held by telephone conference call on January 13, 1981, the Board authorized Seagram to invest up to \$150 million dollars in four companies, *the identities of which were not revealed even to the Board members at that time*,¹⁸ in connection with Seagram's possible interest in a candidate for acquisition. Seagram then immediately began purchasing fifteen million dollars worth of stock in each of the following companies: Santa Fe, Amax, St. Joe, and Kimberly Clark.¹⁹

¹⁷ After this mid-December conversation with Tome, according to Bronfman, during this period "it's possible that [Bronfman] could have mentioned the entire field [of potential acquisition candidates] that we [Seagram] were discussing with basically [the investment banking firm of] Lazard Freres."

¹⁸ But, of course, Tome already had been told of the identities of these four companies as ones that Seagram was considering as a potential target and buying into at the rate of \$15 million apiece.

The identities of these four companies were revealed to the Board at its next regularly scheduled meeting, February 4, 1981.

¹⁹ Kimberly Clark was suggested by Bronfman's brother, who apparently was alone in his interest in that company. Bronfman never seriously considered Kimberly Clark as a takeover candidate.

On January 28, 1981, Seagram determined that it would not proceed with the potential acquisition of Santa Fe.²⁰ Bronfman conveyed this information to Tome by February 6 at the latest. That decision precipitated a sale of Santa Fe stock and options by Finvest Geneva.²¹

The decision not to pursue Santa Fe left only Amax and St. Joe as Seagram's potential takeover candidates. Tome was told of this whittling down of Seagram's possible targets.

Shortly thereafter, in early February, Amax was dropped by Seagram as a potential acquisition candidate. At a lunch that took place sometime on or before February 6, 1981, a partner of Lazard Freres, on behalf of Seagram, approached the Chairman of Standard Oil of California ("SoCal"), which owned 20% of Amax's stock, to ask if SoCal would be willing to sell its interest in Amax. After the Chairman of SoCal told him no, Seagram abandoned any idea of making an acquisition of Amax.

According to Bronfman, "[a]lmost by a process of elimination, that left St. Joe." (emphasis added). Bronfman disclaimed a "clear" recollection of whether he told Tome of Seagram's discontinued interest in Amax: "I'm sorry, it's fuzzy."²² Of the four possible

²⁰ Finvest Geneva was selling Santa Fe stock and options from late January through mid-February 1981, according to Pignatelli.

²¹ Although Bronfman remembers telling Tome of Seagram's discontinued interest in Santa Fe ("the next time I saw him [Tome], I probably, you know, probably told him we [Seagram] were not going to do the Santa Fe deal."), he is unclear of exactly when that was. It was at least "within the next two weeks..."

It must have been by February 6, at the latest, however, since Bronfman does not remember speaking to Tome from February 6 through March 9, 1981.

²² Even if Tome did not hear of Seagram's discontinued interest in Amax from Bronfman, SoCal's (which already owned 20% of Amax) tender offer for Amax on March 6, 1981 would have informed Tome that Amax was no longer a viable target for Seagram. Thus, in any event, at least several days before Tome purchased St. Joe securities on March 10, he knew that St. Joe was Seagram's only viable, remaining takeover candidate.

targets in which Seagram had made an initial and token investment of fifteen million dollars, only St. Joe remained as a potential acquisition candidate for Seagram.

Bronfman asked Lazard Freres to find out as much information as possible about St. Joe and to come up with an evaluation. By February 25, 1981, Bronfman had decided that Seagram would go ahead with a tender offer for the acquisition of St. Joe.

One small diversion developed, but only momentarily. At the suggestion of an investment banker, to canvass the possibility of a "joint venture" arrangement with Santa Fe, Bronfman met for lunch on February 26 in Chicago with the Chairman and Chief Executive Officer of Santa Fe, John Reed. That meeting, however, was unsuccessful.

Seagram tried to keep its interest in St. Joe secret from the marketplace. The market activity in St. Joe securities from January through early March 1981 indicates that Seagram's efforts were largely successful; the value and price for St. Joe securities remained relatively flat. Indeed, Salomon Brothers & Co., a highly knowledgeable New York broker-dealer, executed sales of a vast block of up to one million St. Joe shares on behalf of an institutional client during the two weeks prior to, and including March 9, 1981, when the price range was \$25 to \$30 per share. Had there been any indication abroad that a hostile tender bid to take over St. Joe was expected by the market, Salomon Brothers surely would have advised their client to hold, rather than sell, such a large position.

For several months prior to early March, the average daily volume of trading in St. Joe options on the Philadelphia Exchange had been only about 254 options. By Thursday, March 5, 1981, there was no trading in the March 1981 options of St. Joe which were due to expire that month. The average daily volume of trading in St. Joe common stock on the New York Stock Exchange was approximately 50,000 shares. None of this was indicative to any market follower of an impending hostile tender offer.

D. March 9, 1981 And Following

On March 9, Bronfman was in Hilton Head, South Carolina. He was scheduled to leave there by private jet at 3:00 p.m. He accelerated his departure, however, and instead left Hilton Head at 1:00 p.m. to attend a meeting specially called for later in the afternoon in New York, at 5:30 p.m., with several Seagram executives, its investment bankers, and outside counsel to discuss a St. Joe tender. His bankers were concerned with insuring secrecy of the tender plans afoot by taking early action.

Upon his return to his office in New York, before the 5:30 p.m. meeting, Bronfman received a telephone call from Tome who was also in New York (since Sunday, March 8) at the time. The reason given by Tome for the telephone call was to invite Bronfman to dinner for the following evening, March 10.

Bronfman declined Tome's dinner invitation on the grounds that he "was going to be in Montreal for a directors' meeting." According to Bronfman, *Tome then asked Bronfman*, "[a]re you have a [Seagram] Board meeting in Montreal?"

Armed with his prior knowledge that St. Joe was Seagram's only remaining, viable takeover possibility and with the information he had just obtained from Bronfman in their March 9 phone conversation indicating, from the background of a search for a target, that some official action on corporate matters was imminent, and that Bronfman was on his way to a Board meeting, all signals of important business at hand, Tome decided to concentrate in one day frenzied buying of an enormous quantity of call options on St. Joe stock and of the stock itself; he also tipped others to do likewise. The circumstances were such that Tome reasonably inferred that a vote on a tender proposal was imminent. Tome's immediate conduct confirmed that he was not merely speculating on what was afoot; the extraordinary scope of his financial activities on the next morning was beyond any notion of rational, normal trading. The facts and circumstances lead to the ineluctable inference, which the Court draws, that Tome had obtained material non-public information in confidence from Seagram that it intended to make a tender offer for St. Joe.

Beginning 8:55 a.m. on March 10, Tome, from New York, feverishly placed overseas orders for St. Joe call options to be executed on the Philadelphia Exchange for the accounts of NICO, TFCO, and Finvest Panama. In addition, by 12:35 p.m., Tome had urged others, *i.e.*, clients and business associates, through overseas calls to Europe on at least fourteen separate occasions, to purchase St. Joe securities on American Exchanges.

Before the market opened on March 10, Tome called BSI three times, at 9:13 a.m., 9:26 a.m., and 9:51 a.m., speaking for 4 minutes, 11 minutes, and 3 minutes respectively. He placed the following orders for options²³ to purchase St. Joe stock on behalf of NICO, TFCO, and Finvest Panama through their trading accounts at BSI, spurring on the BSI broker "to rapidly pass the order":

Account	Quantity	Series		Limit Per Underlying St. Joe Share ²⁴
NICO	50	March	\$25	\$3.00
	200	March	\$30	.75
	50	June	\$25	5.00
	50	June	\$30	2.50
TFCO	50	March	\$25	\$3.00
	200	March	\$30	.75
	50	June	\$25	5.00
	50	June	\$30	2.50

²³ Each option gives the purchaser the right to purchase 100 shares of stock on terms provided by the option "series" purchased. The "series" indicates the time at which the option expires and the price at which it is exercisable. So, in this context, purchase of 50 March \$25 options gives the purchaser the option through March 1981 to buy 5,000 St. Joe shares at \$25 per share.

²⁴ This "limit per underlying share" is the maximum price Tome was willing to pay for the option. Since one option represents the right to purchase 100 shares at a future date for a fixed price, a limit of \$3.00 per underlying share would result in a maximum price to buy the one option of 100 shares x \$3.00, or \$300.

<u>Account</u>	<u>Quantity</u>	<u>Series</u>	<u>Limit Per Underlying St. Joe Share²⁴</u>
Finvest			
Panama	100	March \$25	\$3.00
	400	March \$30	.75
	100	June \$25	5.00
	100	June \$30	2.50

Tome called BSI three additional times that day, at 11:07 a.m., 11:51 a.m., and 12:32 p.m., speaking for 6 minutes, 1 minute, and 1 minute respectively. During these calls, approximately two hours after his initial calls to BSI, as the market price began to strengthen from the impact of a buying spree, Tome authorized an increase in the limits on the options previously ordered:

<u>Series</u>	<u>Original Limit</u>	<u>New Limit</u>
March \$25	\$3.00	\$5.00
March \$30	.75	2.00
June \$25	5.00	7.00
June \$30	2.50	4.00

At the same time, Tome furnished BSI with a $\frac{1}{4}$ point discretion and reduced the order for March \$30 call options from 800, total, to 400 contracts.

On March 10, through its account at A.G. Becker, a U.S. securities brokerage company, BSI made the following St. Joe option purchases as a result of Tome's order:

<u>Total Quantity (NICO, TFCO and Finvest Panama)</u>	<u>Series</u>	<u>Average Option Price Per Underlying St. Joe Share</u>
200	March \$25	\$5.25
455 ²⁵	March \$30	2.15
200	June \$25	7.23
200	June \$30	4.22

²⁵ Although Tome had reduced the options ordered in this series from 800 to 400, BSI actually obtained executions on 455. Tome accepted the extra 55 options BSI obtained.

These 1,055 options gave the purchaser the right to purchase a total of 105,500 shares of St. Joe common stock for prices of either \$25 or \$30 per share, depending on the series purchased.

Also on March 10, Tome called Finvest Geneva twice, at 10:30 a.m. and at 10:54 a.m., speaking for 8 and 12 minutes respectively. On March 10, a Finvest Geneva representative, undoubtedly at Tome's direction, placed an order through Baird-Patrick to buy 3,000 St. Joe shares of common stock on the New York Stock Exchange for Finvest Panama's account at BSI. That order was executed at \$30 per share and delivery was made to BSI against payment from BSI's account at Irving Trust Company.²⁶

Two thousand of the three thousand St. Joe shares of stock purchased for the account of Finvest Panama on March 10 were sold for approximately \$94,000, netting an overnight profit of approximately \$34,000. The remaining one thousand St. Joe shares subsequently were exchanged for 1,200 shares of Fluor Corp. The proceeds of the sale and the 1,200 shares are frozen in BSI's account at Irving.

In addition to Tome's direct purchases, his telephone calls caused and resulted in tippee transactions on a grand scale. At 8:55 a.m. on March 10, Tome called his client Banque du Rhone, a Swiss bank in Geneva, Switzerland, speaking for 17 minutes. About three hours later, at 11:58 a.m., Banque du Rhone purchased 200 St. Joe shares and 50 St. Joe call options, at a total cost of \$16,750. The subsequent sale of these securities resulted in proceeds of \$114,756, with a net profit of \$98,006.

At 10:17 a.m. On March 10, Tome called Leati of Lombardfin S.p.A. in Milan, Italy, speaking for 5 minutes.²⁷ Leati admits that in this telephone call Tome told Leati "I'd buy [St. Joe]." In view of the interrelationships, that expression was the equivalent of a virtual direction.

²⁶ This purchase was confirmed by telex to BSI from Finvest Geneva on March 11, 1981.

²⁷ Tome also called Lombardfin at 12:35 p.m. on March 10, speaking for 4 minutes.

Two minutes after hanging up on Tome's phone message, at 10:24 a.m., Leati, without first consulting his clients, began buying St. Joe securities on behalf of Lombardfin clients through their Lombardfin accounts. Before this first trade, Lombardfin S.p.A. had never traded even one single share of St. Joe securities. By the end of the day, however, Leati had purchased more than 40,000 shares for the following accounts and the positions were shortly thereafter liquidated with the profit results indicated:

Account Name	First Trade	Quantity ²⁸	Cost	Liquidation Proceeds
Credit Suisse				
Lausanne	10:24 a.m.	10,000 S	\$294,375	\$481,250
Osiris Ltd.	10:26 a.m.	500 O	168,237	835,062
Credito Svizzero				
Chiasso	11:45 a.m.	8,000 S	240,437	360,500
Unione di Bache Svizzere	1:00 p.m.	3,000 S	91,875	137,375
Banque Pictet	2:23 p.m.	3,000 S	90,375	137,375
Banque Privee	3:34 p.m.	5,000 S	150,625	235,812
Credito Svizzera				
Lugano	3:59 p.m.	9,200 S	276,850	437,200
Lombardfin	No Time			
Securities	Stamp	2,000 S	60,750	93,875
TOTALS		40,200 S & 500 O	\$1,373,524	\$2,719,449

Deducting total cost from total proceeds, these transactions resulted in a profit of \$1,345,925 for these accounts.

At 10:24 a.m. on March 10, about two minutes after getting off the phone with Leati at Lombardfin, Tome called Cramer, a Swiss bank in Geneva, Switzerland, and a Tome client, speaking

²⁸ The letter "S" designates St. Joe shares, and the letter "O" designates St. Joe call options.

for 5 minutes. *Twelve minutes* later, at 10:41 a.m., Cramor began buying St. Joe securities. It purchased 100 St. Joe call options and 1,000 St. Joe shares, at a total cost of \$50,012. The subsequent sale of these securities shortly thereafter resulted in proceeds of \$183,500, with a net profit of \$133,488.

At 11:15 a.m. on March 10, Tome called Compagnie de Banque et d'Investissements ("CBI"), a Swiss bank in Geneva, Switzerland, a Tome client, and a partner in Tome's Finvest organization, speaking for 1 minute. Less than two hours later, at 1:00 p.m., CBI ordered 150 St. Joe call options and 1,100 St. Joe shares, at a total cost of \$64,837. The subsequent sale of these securities shortly after the purchases resulted in proceeds of \$234,000, with a net profit of \$169,000.

As noted previously, on March 10, Tome called Finvest Geneva twice, once at 10:30 a.m., speaking for 8 minutes, and once at 10:54 a.m., speaking for 12 minutes. Shortly after each of these calls, two of Tome's clients, Banque Gutzwiller ("Gutzwiller") and Trade Development Bank ("TDB") began buying St. Joe securities.

At 10:40 a.m. on March 10, Gutzwiller ordered 2,000 St. Joe Shares, at a total cost of \$59,250. The subsequent sale of these securities resulted in proceeds of \$90,737, with a net profit of \$31,487.

At 12:02 p.m. on March 10, TDB ordered 13,000 St. Joe shares, at a total cost of \$390,750. At 6:39 a.m. on March 11, Tome called TDB, speaking for 10 minutes. Subsequently, beginning at 2:55 p.m. on March 11, TDB sold its St. Joe shares for proceeds of \$597,675, with a net profit of \$206,925.

What method Tome used to convey his inside information to Gutwiller and to TDB cannot be stated with certainty. Under the circumstances and facts of this case, however, it is reasonably inferable that Tome did convey his inside information to them. These two banks were clients that Tome brought over to Baird-Patrick, with Tome listed as representative for the accounts. Both banks began trading in St. Joe securities at exactly the same time

as the banks Tome had called directly. Both banks began trading very shortly after Tome's calls to Finvest Geneva. Gutzwiller placed its order two minutes after Tome had completed his first call to Finvest Geneva; TDB placed its order less than one half hour after Tome completed his second call to Finvest Geneva. The evidence shows that Tome called many of his other clients directly on March 10 to tell them to buy St. Joe securities. Tome called TDB directly at 6:39 a.m. on March 11, just hours before the Seagram tender offer was publicly announced. Unquestionably, Tome was in direct contact with at least TDB during this crucial interval.

Despite the uncertainty over *how* the inside information was conveyed by Tome to Gutzwiller and to TDB, it is reasonably inferable that it *was* conveyed. Moreover, this uncertainty over *how* is largely due to Tome's refusal to testify in this action, by invoking his Fifth Amendment privilege against self-incrimination. While Tome has a right to remain silent and thereby to not inculcate himself and to avoid confrontation therewith in the criminal action, he is not entitled to profit by his silence in this civil action. Therefore, to the extent necessary, this Court is justified in drawing an adverse inference from Tome's assertion of his Fifth Amendment privilege in this civil action.²⁹ This Court finds that Tome conveyed the inside information that he possessed to Gutzwiller and to TDB, and that they subsequently traded and profited personally on that information. Consequently, Tome is liable to account for their profits obtained from these transactions.

When aggregated, the activities of Tome, as recited above, directly and indirectly, accounted for a significant portion of the volume of St. Joe option transactions executed on the Philadelphia Exchange on March 10:

²⁹ For a discussion of the legal justification for drawing an adverse inference from Tome's assertion of his Fifth Amendment privilege in this civil action, see the separate memorandum on evidentiary issues raised in this case.

Series	Total St. Joe Calls Purchased On March 10	Total St. Joe Calls Purchased By Defendants March 10	Percentage of Total Calls On St. Joe Represented By Defendants' Purchases
March \$25	285	200	70 %
March \$30	2334	705	30 %
June \$25	1334	200	15 %
June \$30	740	350	74 %
June \$35	463	50	11 %
TOTALS	5,626	1,855	33 %

In addition to options on 185,500 shares of St. Joe common stock, Tome and his satellite purchasers accounted for the purchase of at least 60,500 St. Joe shares, 10.67 % of the total volume in St. Joe stock on the New York Stock Exchange on March 10.

On March 10, 1981, at 7:00 p.m., an unscheduled special meeting of the Seagram parent company Board of Directors was held in Montreal, Canada. This special meeting was called on short telephone notice according to the Board minutes. Bronfman, in common with the other directors, unaware of Tome's feverish trading activity earlier in the day, attended this special meeting.

Bronfman's deposition testimony was content to characterize this special meeting on March 10 as merely an "acceleration" of the "regularly scheduled" Board meeting, which was accelerated from March 11 in response to suggestions of the investment bankers concerned with maintaining confidentiality of the ongoing preparation of the tender offer to be voted on by the directors as well as probably dismayed at the market activity in the St. Joe stock on March 10. Bronfman's uncertain recollection was that the *decision* to accelerate was made at lunch on March 10, but there was no luncheon — if the recollection were true, thirteen of the fifteen Seagram parent company Directors, including eight of the ten outside Directors, and the substantial coterie of

investment bankers, consultants, engineers, and lawyers who showed up at the meeting, came to Montreal a day earlier than the fixed meeting date on *at most* six or seven hours notice before the meeting began. There was no testimony that pinpointed when he *first considered* accelerating the meeting, *i.e.*, whether accelerating the Board meeting was considered before or after he spoke to Tome on March 9 and turned down a dinner engagement for the evening of the special meeting.

On March 10, 1981, the parent company authorized Seagram to make its tender offer for the shares of St. Joe.

The defendants presented a witness with a view to explaining the extraordinary 50 % surge of the market price on March 10th 1981. Mr. Marc Cohen, an analyst in mining industries for the brokerage firm of Kidder, Peabody held to the dubious belief that events over many prior months caused the explosion. When questioned about what material non-public information might catalyze what occurred, he conceded that an awareness that a special meeting of the Seagram Board was about to take place would have been material, non-public information in light of the contemporaneous facts and circumstances and inferentially might account for what had happened.

On March 11, before Seagram's announcement of the St. Joe tender offer, Tome called BSI twice, at 6:23 a.m. and 6:25 a.m., speaking for 1 and 2 minutes respectively. At 8:00 a.m., BSI called Tome back. During this conversation, Tome instructed BSI to place an order for an additional 2,055 St. Joe call options *without price limit at the market*. While BSI was attempting to place this order, Tome anxiously stayed on an open telephone line to BSI for confirmation. BSI informed Tome that 2,000 call options was the floor trading limit on the Exchange. Tome then reduced his call option purchase order to 945 call options.

Again that morning, before the Seagram tender offer for St. Joe was publicly announced, Tome again placed overseas calls to two European clients. At 6:04 a.m. he called CBI, speaking for 1 minute. At 6:39 a.m. Tome called TDB, speaking for 10 minutes.

At 9:22 a.m. on March 11, the Seagram tender offer for St. Joe was publicly announced. The announcement resulted in a delay in the opening of trading for St. Joe securities. In consequence, the large call option orders Tome placed on the morning of March 11 were never executed on the Exchange.

At 10:30 a.m. on March 11, a so-called "regularly scheduled" Board meeting of the Seagram parent company was held in Montreal pursuant to a notice of meeting that had been forwarded to all Directors on February 23, 1981.

After the meeting on March 11, Bronfman returned to New York from Montreal. Through arrangement prior to March 9, 1981, between their wives, Bronfman and Tome met and went in the evening of March 11th to see the play they had invested in, "Sophisticated Ladies."

That evening, Bronfman discussed Seagram's tender offer for St. Joe with Tome. Bronfman discussed his telephone conversation with the St. Joe management, whom he had called just prior to Seagram's public announcement of the St. Joe tender to advise them of the impending offer. Bronfman discussed with Tome the price Seagram had tendered and speculated to Tome on Seagram's chance of success. In addition, Bronfman disclosed the timetable for the St. Joe tender and the behind-the-scenes arrangements for Board meeting schedule changes.

Despite Bronfman's confidences and discussions with Tome on the topic of the St. Joe tender offer that evening, Tome was eloquently silent and mentioned absolutely nothing to Bronfman about Tome's massive orders, trades, telephone calls overseas, and exhortations to others in regard to St. Joe securities.

Beginning on March 12, 1981, Tome instructed BSI immediately to liquidate and cash in the St. Joe option positions acquired on March 10. Specifically, at about 8:24 a.m., Tome called BSI, speaking for 9 minutes, and instructed it to sell all March options he had purchased for the accounts of NICO, TFCO, and Finvest Panama. At 8:43 a.m., Tome called Banque du Rhone, speaking for 6 minutes. Shortly thereafter, Banque du Rhone cashed in its purchases.

On March 12, Bronfman gave a dinner party in Tome's honor for twenty people at Bronfman's house. Once again, Bronfman talked to Tome about the Seagram tender offer for St. Joe. Again, Tome maintained total secrecy and made no mention to Bronfman about his activities in St. Joe securities in the prior two days.

On March 13, at 8:47 a.m., Tome called BSI, speaking for 11 minutes, and instructed it to sell the 50 June \$25 options and 50 June \$30 options he had acquired on March 10. On that same day, news of the SEC inquiry into possible insider trading on the Seagram bid for St. Joe was publicly disseminated.

Tome decided it was time to leave New York. Although he had reservations through March 18 at his hotel in New York, Tome cut short his visit to the United States and returned on March 14 to Switzerland.

On March 15, 1981, Tome, in Geneva, called BSI and requested that they rearrange the option purchases to make it appear that Finvest Panama had not purchased any of the St. Joe options. He suggested that Finvest Panama's purchases of March options be reallocated to NICO and of June options be reallocated to TFCO. The ostensible reason for this falsification and switch was to "secure greater confidentiality within his organization." After a series of meetings, BSI vehemently declined to change its records of the transactions as they were effected. BSI reported to Tome that its account entries were "unalterable" and Tome's requests to change the record were rejected.

The SEC filed this suit on March 27, 1981. The SEC initially had difficulty in identifying so shortly after the trading activity the foreign nationals who made the trades, and the defendants were initially identified by category, not by name. As it became clear exactly who had engineered the St. Joe trades, their names were added by amendment to the title of the lawsuit.

BSI, the Swiss bank, and Irving Trust Company of New York, were the only defendants named in this suit on March 27, 1981. Proceeds of the illegal trading, as later described herein, were in the possession of Irving Trust, and under the control of BSI.

The accounts for which trades were made through the Lugano branch of BSI were identified only as those of "Unknown Purchasers."

As a result of the liquidation of the options transactions through BSI, approximately \$1,825,000 (less commissions) was credited to BSI's account at Irving Trust Company, at the direction and on behalf of Tome, NICO, TFCO, and Finvest Panama. Of this sum, approximately \$1,442,000 represented profit.

Despite the fact that Tome's name had not been mentioned in any public documents as being implicated in insider trading, on Monday, March 30, 1981, after hearing of this suit, Bronfman immediately telephoned Tome. Bronfman called Tome because he was concerned that:

perhaps he [Tome] had done something. I wanted to make doubly sure he hadn't. Because the only person I knew in Switzerland that would have any knowledge one way or another of anything that was going on, at least for me, was Mr. Tome.

Bronfman was unable to reach Tome.

From Zurich, Switzerland, Tome returned the call by telephoning Bronfman at his apartment that same night at approximately 7:20 p.m. Tome said that he was sorry that Bronfman had called him earlier. He then told Bronfman the first of several boldfaced lies:

You know, I've been in this business [*i.e.*, securities] for 20 years and I know what to do and what not to do. And clearly I certainly didn't do anything.... But, it's a little more complicated than that and I will see you in New York next week.

A week later, on Monday, April 6, at approximately 5:30 p.m., Tome dropped by Bronfman's apartment in New York unexpectedly. Tome lied again and told Bronfman that, in his absence from Geneva, "one of his [Tome's] people" had put through an order

for 3,000 shares of St. Joe stock but that "he [Tome] hadn't personally placed the order."³⁰ Bronfman asked Tome, point blank, "Were those shares in any way beneficially owned by you or members of your family?" Tome responded unequivocally, "No."

Bronfman and Tome met again the next morning, April 7, at 10:00 a.m. at Bronfman's office. Bronfman's attorney was present at that meeting. This time Tome had an attorney present, who arrived at approximately 10:20 a.m. Bronfman and his attorney made it clear to Tome and his attorney that any conversations they would have that day would be reported to the SEC.

At this meeting, Tome "reiterated that none of [the 3,000 shares of St. Joe stock purchased] had gone into his accounts" and that neither he, his wife, his children, nor any members of his family had any beneficial interest in St. Joe stock. He again said that "his clerk" had heard rumors about St. Joe and had decided, on his own to buy 3,000 shares and "put them in various accounts."

In addition, Tome asserted flatly that he had "absolutely nothing to do" with the St. Joe option purchases on March 10. In fact, in response to a question from Bronfman's lawyer concerning whether Tome had any reason to believe that the beneficial holder of the 3,000 St. Joe shares was in any way related to the beneficial holders of the St. Joe options involved in this suit, Tome said that "[n]o, he had no reason to think so." Tome disclaimed any direct or indirect beneficial interest in any option trades. He termed it a "coincidence" that on March 10th, in addition to the 3,000 shares, defendant BSI also purchased 1,055 St. Joe call options on 105,500 shares of stock for prices of either \$25, \$30, or \$35 per share.

The canards were ultimately exploded. After the SEC's diligent investigation uncovered irrefutable evidence of Tome's involvement in the St. Joe option and stock trades, Tome's counsel conceded on the record that Tome has a beneficial interest in St.

³⁰ Tome repeated a slightly different version of this lie to the head of Baird-Patrick, the U.S. brokerage firm with which Tome was associated.

Joe stock purchases.³¹ At trial, Tome's counsel and the Court engaged in the following colloquy:

Counsel: ... Tome was responsible for purchasing stock on March 10. That's not denied. There was an announcement —

The Court: You mean it's not any longer denied?

Counsel: It is not denied, your Honor.

The Court: He falsified about that initially, didn't he?

Counsel: I believe that the testimony of Bronfman indicates that he [Tome] was not candid about that fact, [J]udge.

The Court: That's the understatement of the year.

On April 8, 1981, Tome called Bronfman from Geneva, Switzerland, and in a belligerent tone accused Bronfman of getting him into this "mess." Tome claimed that Bronfman's lawyers were going to protect Bronfman and leave Tome "out in the cold." When Tome continued to talk to Bronfman in this belligerent tone, Bronfman terminated the call. Fifteen minutes later, Tome called him back, this time very distraught. Tome was concerned with the possibility of going to jail because if he did "his career would be finished."³²

Sometime thereafter, Bronfman, strangely enough, asked his wife to call Tome's wife to tell her "Don't worry. We love you.... The reason Edgar's [Bronfman] not calling you is because he's being advised not to. But he still loves you."

³¹ Tome's counsel now concedes, in the face of irrefutable proof, that Tome had a beneficial interest in the NICO account.

³² Specifically, Tome told Bronfman that if Tome did not talk to the SEC, he could go to jail in the United States; conversely, if he did talk to the SEC, he could go to jail in Switzerland for violating Swiss secrecy laws.

E. Leati's Disclosures

Leati himself admits that in a telephone conversation on March 10, 1981, Tome advised him to purchase St. Joe securities. Leati states that he got the "hint" to buy St. Joe from Tome when Tome said "I'd buy [St. Joe]." Leati claims, however, that he never heard of Seagram, as a company, until the official announcement of the tender offer nor did he know of Tome's (and Finvest Geneva's) relationship with Seagram. He claims that after Tome gave him the "hint" on St. Joe, he bought the stock not because of any knowledge of an imminent Seagram tender offer but because "the volume [of trading in St. Joe stock] was increasing in the days immediately prior to the transaction." In essence, Leati would have this Court believe that although he received the "hint" to buy St. Joe from Tome, Leati engaged in some sophisticated, independent market research and analysis after speaking to Tome and before making the actual decision to purchase St. Joe securities for the accounts of Lombardfin S.p.A.'s clients. That notion is unworthy of belief.

In fact, the volume was not steadily increasing in the week and days immediately prior to Lombardfin S.p.A.'s March 10 purchases.³³ More significantly, however, Leati placed the first order for St. Joe stock, 10,000 shares, approximately *two minutes* after finishing his telephone conversation with Tome.³⁴ Leati could not have had time to investigate the St. Joe stock before trading. In

³³ At trial, Kevin Fechan, the New York Stock Exchange specialist in St. Joe during this period of time testified as follows:

The Court: ... so you had one day [Thursday, March 5] where there was a [trading] bulge and the other days generally subnormal is that the story of that week [Monday, March 2 through Friday, March 6, 1981]?

Witness: That's the story of that week.

³⁴ Tome's first call to Leati on March 10 was placed at 10:17 a.m. and lasted approximately five minutes. Leati's first trade *ever* in St. Joe securities, which he placed for the account of Credit Suisse Lausanne, was placed at 10:24 a.m.

this regard, it is highly significant that before March 10, 1981, Lombardfin S.p.A. had never traded even one single share of St. Joe stock. On March 10, 1981, however, it traded more than 40,000.

Not surprisingly, Csopey, Leati's former partner at Lombardfin S.p.A., tells a very different – and more believable – version of what caused Lombardfin S.p.A. to trade in St. Joe securities on March 10.³⁵ In his testimony, Leati was evasive and belligerent, often berating the attorney for asking a particular question. In sharp contrast, Csopey's testimony was careful and credible.³⁶

Csopey was in charge of the Rome office of Lombardfin S.p.A.'s Italian domestic subsidiary – Leati was in charge of the Milan office – and thus was usually in Rome. On March 10, 1981, however, Csopey was in Milan to visit customers and to attend a Board meeting the next day.

While in the Milan office on March 10, Csopey and his then partner, Leati, had a private conversation in Leati's office. Leati

³⁵ For a discussion of defendants' hearsay objections to portions of Csopey's testimony, see the separate memorandum on evidentiary issues.

³⁶ Moreover, Leati's testimony was taken in Italy under the restrictive Letter Rogatory procedure and Csopey's in New York under the much more liberal standard applicable under the Federal Rules of Civil Procedure.

Defendants, through innuendo, have attempted to attack Csopey's credibility by hinting at certain events surrounding a 1984 struggle for control of Lombardfin S.p.A. between Leati and Csopey. In September 1985, at his deposition in this country, Csopey denied categorically making any threats to discuss the St. Joe matter with the SEC if Leati did not sell his interest in Lombardfin S.p.A. to Csopey. Rather than cross-examining Csopey specifically on this point, bringing out whatever evidence Tome's counsel had to support such an accusation, and getting Csopey's response or explanation thereto, Tome's counsel *chose* to raise the issue collaterally, through the hints and specters of witnesses not available in this Court for testimony under the Federal Rules. Those 1984 events and defendants' innuendoes do not detract from the circumstantial credibility of Csopey's recital of the events of 1981. The credibility of Csopey's main accuser, Mrs. Arbucias, is seriously impaired in the totality of the evidence submitted and her allegations are not worthy of belief.

told Csopey that Tome had called Leati from New York.³⁷ "Leati [] had been advised by Tome ... [t]hat Seagrams [sic] would make, in the next few days, make a tender offer for St. Joe Minerals." Leati said that, in exchange for \$200,000, Tome was passing this information to Lombardfin S.p.A. for Lombardfin to take advantage of for itself and for its customers. This prospective payment to Tome was contingent upon there being a takeover and was to come not from Leati nor from Lombardfin S.p.A., but from those individuals profiting from Tome's information.

Leati discussed the reliability of Tome's information with Csopey, mentioned that Tome was a consultant to Seagram, and stated that "since Tome claimed to have a close personal relationship to Seagrams [sic], that this [information] could well be true."

Leati told Csopey that he had already bought some stock and options in St. Joe that day while Csopey was not in the office. Leati said that he had not spoken to any customers before placing trades on their behalf in St. Joe on March 10. Indeed, Csopey knew from his own experience that mobilizing so many trades in so short a period of time necessitated Leati to be acting on his own discretion, without first checking with customers.

At the end of this conversation, Leati, considering additional purchases of St. Joe securities, said to Csopey "Let's give it a try." In fact, Leati placed additional orders for St. Joe securities on March 11 before the New York Stock Exchange opened, but these orders could not be executed because the market opening in St. Joe was delayed by the Seagram tender offer announcement.

The next day, the Board meeting of Lombardfin S.p.A., and its Italian subsidiary, was interrupted by news of the Seagram tender offer for St. Joe. The discussion at the meeting then turned to St. Joe, with comments ranging from an estimate of the

³⁷ Like many of Csopey's other statements, this statement, which Csopey would have no reason to know except if Leati actually did tell him, is fully corroborated by independent evidence, i.e., telephone records and Leati's own admission.

stock's opening price to regulatory consequences for the prior day's trading. Leati explained to the board members, who were not intimately familiar with the mechanics of New York Stock Exchange trading, what was going on. In discussing the regulatory consequences, Leati admitted that the firm had committed a securities violation by trading on inside information but apparently downplayed the risk of being caught by remarking that Lombardfin S.p.A. had accounted for only a "small fraction" of the previous day's total trading volume. Csopey does not remember if, at that meeting, Tome was identified to the Board as the person providing the inside information. He was, at least, identified to them later.

On March 11, 1981, Leati told Csopey that Tome and Leati had exchanged telephone calls and Tome had told him that "[t]he launch of the [Seagram] takeover bid had been anticipated [*i.e.*, accelerated] due to market action."

Throughout 1981, after the SEC had instituted this lawsuit, Tome regularly visited Lombardfin's office in Milan. When he was in Milan, Csopey and Tome had discussions about this lawsuit in general, particularly how large the legal fees were for all people concerned. Subsequently, Leati told Csopey that Tome had pressed Leati for contributions to the legal fees and to a pool which would settle the case. In fact, when Lombardfin S.p.A. itself began running up substantial legal fees in connection with this case Leati told Csopey that Leati should have anticipated these legal expenses and "taken account" of them in the money given to Tome for providing the inside information.

II. INSIDER TRADING

The SEC brings this civil insider trading action, authorized by Section 21(d) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. § 78u(d), seeking an injunction and other ancillary relief, including disgorgement of ill-gotten gains, against defendants based on defendants' violations of the antifraud provisions of the securities laws and regulations. Subject-matter jurisdiction is based on Sections 21(e) and 27 of the Exchange Act, 15 U.S.C. §§ 78u(e) and 78aa. For the reasons shown hereafter, the SEC is entitled to prevail.

The federal securities laws do not contain an express definition of insider trading. Instead, liability for insider trading has grown out of the antifraud provisions of the securities laws and regulations, primarily Section 10(b) and Rule 10b-5. As the Supreme Court has made clear, however, "not every instance of financial unfairness constitutes fraudulent activity under § 10(b)." *Chiarella v. United States*, 445 U.S. 222, 232, 100 S.Ct. 1108, 1116-17, 63 L.Ed.2d 348 (1980). The gravamen of an insider trading violation under these provisions is breach of a fiduciary or similar duty of trust and confidence arising from some relationship. An individual trading on inside information in breach of such a duty, without prior disclosures,³⁸ commits fraud within the meaning of Section 10(b) and Rule 10b-5.

The term "insider trading" actually is a misnomer, only imperfectly describing the proscribed conduct, since liability under the securities laws can extend to those who are not insiders, as that term is commonly understood (*e.g.*, directors and officers of the corporation, *see Moss v. Morgan Stanley Inc.*, 719 F.2d 5, 10 & n.8 (2d Cir. 1983), *cert. denied sub nom.*, *Moss v. Newman*, 465 U.S. 1025, 104 S.Ct. 1280, 79 L.Ed.2d 684) (1984)), if these "outsiders" either become "temporary insiders"³⁹ of the corporation by legitimately being given access to confidential corporate information solely for corporate purposes, *Dirks v. SEC*, 463 U.S. 646, 655 n.14, 103 S.Ct. 3255, 3262 n. 14, 77 L.Ed.2d 911 (1983), or become "tippees" by receiving inside information *improperly*. *Id.* at 660, 103 S.Ct. at 3264 (emphasis in original). Temporary insiders acquire independent fiduciary duties to the corporation and to its shareholders, and thus commit fraud within the meaning of Section 10(b) and Rule 10b-5 when they breach their

³⁸ If the insider cannot disclose because of a duty not to reveal confidences, he must abstain from trading altogether. *United States v. Chiarella*, 588 F.2d 1358, 1365 & n. 9 (2d Cir. 1978), *rev'd*, 445 U.S. 222, 100 S.Ct. 1108, 63 L.Ed.2d 348 (1980); *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 848 (2d Cir.1968) (*en banc*), *cert. denied sub nom.*, *Kline v. SEC*, 394 U.S. 976, 89 S.Ct. 1454, 22 L.Ed.2d 756 (1969). *See also infra* note 47.

³⁹ The term "temporary insider" apparently was coined in *SEC v. Lund*, 570 F.Supp. 1397, 1403 (C.D.Cal.1983).

fiduciary or similar duty of trust and confidence. Tippees, however, have no independent fiduciary or similar duty of trust and confidence to the corporation or to its shareholders; their liability for insider trading "is derivative from that of the insider's duty." *Id.* at 659, 103 S.Ct. at 3264. If there has been no breach by an insider (*i.e.*, the "tipper") in conveying the inside information to the tippee, there can be no derivative breach by the tippee. *Id.* at 662, 103 S.Ct. at 3265. Even if there has been a breach by the tipper of his fiduciary or similar duty of trust and confidence, the tippee only commits fraud within the meaning of Section 10(b) and Rule 10b-5 if the tippee trades on that inside information when he "knows or should know" that the inside information was conveyed to him in breach of the tipper's duty. *Id.* at 660, 103 S.Ct. at 3264.

Tipplers are jointly and severally liable for the profits obtained (or losses avoided) by their tippees. See *Bateman Eichler, Hill Richards, Inc. v. Berner*, — U.S. —, 105 S.Ct. 2622, 2630, 86 L.Ed.2d 215 (1985) ("A tippee trading on inside information will in many circumstances be guilty of fraud against individual shareholders, a violation for which the tipper shares responsibility.") (emphasis added); *Elkind v. Liggett & Myers, Inc.*, 635 F.2d 156, 169 (2d Cir.1980).⁴⁰ Indeed, the Supreme Court has held that the tipper's conduct, almost invariably, is more culpable than that of the tippee. *Batemen*, 105 S.Ct. at 2630-31. Tipper liability is necessary so that a fiduciary does not attempt indirectly to do that which he may not do directly. *Dirks*, 463 U.S. at 659, 103 S.Ct. at 3264.

Before tipper and tippee liability arises under Section 10(b) and Rule 10b-5, however, there first must be a breach of the

⁴⁰ Expanding on this reasoning, a tipper is liable for profits obtained (or losses avoided) from his tippee's trades, even if the tippee himself could not be held liable for those trades because he did not commit fraud within the meaning of Section 10(b) and Rule 10b-5, *i.e.*, if the tippee did not and should not have known that the information was conveyed in breach of the tipper's fiduciary duty, or because he was not joined as a defendant in the action. See *Texas Gulf Sulphur Co.*, 401 F.2d at 852-53 (tipper held liable for Section 10(b) and Rule 10b-5 violations based on tippees' trades even though tippees not joined as defendants). A tipper's liability is independent, nor derivative, of the tippee's.

insider's fiduciary or similar duty of trust and confidence, satisfying the fraud element. "The test is whether the insider personally will benefit, directly or indirectly, from his disclosure." *Id.* at 662, 103 S.Ct. at 3265. Focusing on objective criteria, the court must find "a pecuniary gain or a reputational benefit that will translate into future earnings." *Id.* at 663, 103 S.Ct. at 3266. As examples of situations satisfying this breach requirement, the Supreme Court noted "a relationship between the insider and the recipient that suggests a *quid pro quo* from the latter or an intention to benefit the particular recipient" and "a gift of confidential information to a trading relative or friend." *Id.* at 664, 103 S.Ct. at 3266 (emphasis in original). Determining whether the insider personally benefits from a disclosure is a question of fact. *Id.*

One relationship giving rise to a duty sufficient to support liability under Section 10(b) and Rule 10b-5 is a fiduciary or similar relationship of trust and confidence between the shareholders of the company whose stock is being traded and the individual trading. This is the relationship the Supreme Court focused on in *Chiarella* and *Dirks*. Recently, however, in actions brought by governmental agencies, the lower federal courts have been extending liability under Section 10(b) and Rule 10b-5 to other relationships, under a "misappropriation" theory.

The common-sense notion underlying the misappropriation theory is that one who misappropriates valuable information for his own benefit, in breach of a fiduciary or similar duty of trust and confidence, has surely committed fraud on the person or entity to whom that duty is owed. The prerequisite for liability under the misappropriation theory is misuse of nonpublic information in breach of a fiduciary or similar duty of trust and confidence to *some* person or entity, although that person or entity need not necessarily be a purchaser or a seller of securities.⁴¹ See

⁴¹ Because of the judicially-created standing requirement limiting private Rule 10b-5 damage claims to purchasers or sellers of securities, *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 737, 95 S.Ct. 1917, 1926, 44 L.Ed.2d 539

(footnote continued)

Report of The Task Force On Regulation of Insider Trading (part 1): Regulation Under The Antifraud Provisions of The Securities Exchange Act of 1934, 41 Bus.Law. 223, 236 (No. 1985) [hereinafter cited as ABA Report]. Thus, under the misappropriation theory, the scope of the duty required to ground liability is no different than the one outlined by the Supreme Court in *Chizrella*, and reiterated in *Dirks*⁴² the person or entity to whom that duty is owed, however, for purposes of liability under Section 10(b) and Rule 10b-5, is not limited solely to shareholders of the corporation whose stock is being traded (*i.e.*, the target company in a takeover situation) or to that corporation itself.

The Second Circuit, by a divided Court, has just held that the fraud element of a 10b-5 violation is satisfied when a defendant newspaper writer misappropriates, and then trades on (or tips others who trade on), nonpublic information of forthcoming articles to be published regarding the subject securities, in breach of a fiduciary or similar duty of trust and confidence to the newspaper. The violators did not breach a duty directly or derivatively to anyone involved in acquiring the securities. *United States v. Carpenter*, 791 F.2d 1024, 1029 (2d Cir.1986) ("the misappropriation theory more broadly proscribes the conversion by

(1975), the extension of liability under Section 10(b) and Rule 10b-5 made possible by the misappropriation theory will be useful only for actions instituted by governmental agencies, such as the SEC under section 21 or the United States Attorney under section 32 of the Exchange Act. Prudent exercise of these governmental agencies' inherent prosecutorial discretion no doubt will limit even further the actions brought under the misappropriation theory.

⁴² In *United States v. Reed*, 601 F. Supp. 685 (S.D.N.Y.) (upholding the sufficiency of an indictment for insider trading on the theory that a son had misappropriated from his father confidential information concerning a forthcoming merger), *rev'd as to venue*, 773 F.2d 477 (2d Cir. 1985), after a scholarly review of the concepts of "fiduciary relationship" and "confidential relationship" as those terms have been understood in the law, *id.* at 703-18, the District Judge concluded that "[t]he repeated disclosure of secrets by the parties or by one party to the other may in the final analysis suffice to support a finding of a confidential relationship" sufficient to ground liability under Section 10(b) and Rule 10b-5. *Id.* at 717. Determining whether a confidential relationship exists is a question of fact. *Id.*

'insiders' or others of material non-public information in connection with the purchase or sale of securities.") (emphasis in original).

This "misappropriation" theory of liability under Section 10(b) and Rule 10b-5 first appeared in the case law in *Chiarella v. United States*, 445 U.S. 222, 100 S.Ct. 1108, 63 L.Ed.2d 348 (1980), when the government urged the Court to affirm Chiarella's conviction for insider trading on the alternative basis that Chiarella, an employee of a financial printer employed by an acquiring corporation involved in a tender offer, violated Section 10(b) and Rule 10b-5 when he breached his duty of confidentiality to the acquiring corporation by acting upon information he received by virtue of his employee status. *Id.* at 235, 100 S.Ct. at 1118.

The Court held that "it need not decide whether this theory has merit for it was not submitted to the jury." *Id.* at 236, 100 S.Ct. at 1118. Four Justices, however, explicitly voiced their view that a defendant violates Section 10(b) and Rule 10b-5 when misappropriating, and then trading on (or tipping others who trade on), nonpublic information in breach of a fiduciary or similar duty of trust and confidence. *See id.* at 245, 100 S.Ct. at 1123 (Burger, C.J., dissenting) (Chiarella "misappropriated — stole to put it bluntly — valuable nonpublic information entrusted to him in the utmost confidence."); *id.* at 239, 100 S.Ct. at 1120 (Brennan, J., concurring); *id.* at 245, 100 S.Ct. at 1123 (Blackmun, J., joined by Marshall, J., dissenting). More recently, in *Bateman, Eichler, Hill Richards v. Berner*, — U.S. —, 105 S.Ct. 2622, 86 L.Ed.2d 215 (1985), seven Justices joined an opinion stating that "[w]e also have noted that a tippee may be liable [under Rule 10b-5] if he otherwise 'misappropriate[s] or illegally obtain[s] the information.'" *Id.* at 2630 n. 22 (quoting *Dirks v. SEC*, 463 U.S. 646, 665, 103 S.Ct. 3255, 3265, 77 L.Ed.2d 911 (1983)). The two justices who did not join the *Bateman* opinion (Justice Marshall did not participate and the Chief Justice concurred) were ones who in *Chiarella* had explicitly approved the misappropriation theory.

Although the Supreme Court has not yet explicitly decided the validity of the misappropriation theory of liability under Section

10(b) and Rule 10b-5, all nine current members of the Court appear to support the misappropriation theory.

Significantly, in the interim between the *Chiarella* and the *Bateman* decisions, the Congress has expressly approved the misappropriation theory as being consistent with the purposes of the antifraud provisions of the securities laws. See *Carpenter, supra*, at 1030 (finding "persuasive" the congressional intent expressed in the ITSA). In the House Committee Report accompanying the Insider Trading Sanctions Act of 1984 ("ITSA"), Pub.L. No. 98-376, 98 Stat. 1264 (codified in scattered sections of 15 U.S.C.) (there was no Senate report), the Congress, citing with approval the Second Circuit's decision in *United States v. Newman*, 664 F.2d 12 (2d Cir. 1981), *conviction aff'd without published opinion*, 772 F.2d 729 (2d Cir.), *cert. denied*, 464 U.S. 863, 104 S.Ct. 193, 78 L.Ed.2d 170 (1983), which upheld the legal sufficiency of a criminal indictment under Section 10(b) and Rule 10b-5 based on the misappropriation theory, stated that:

[I]n certain widely-publicized instances, agents of tender offerors and persons contemplating a merger or acquisition have used for personal gain information entrusted to them solely for a business purpose. Such conversion for personal gain of information lawfully obtained abuses relationships of trust and confidence and is no less reprehensible than the outright theft of nonpublic information. In other areas of the law, deceitful *misappropriation* of confidential information by a fiduciary, whether described as theft, conversion, or breach of trust, has consistently been held to be unlawful. The Congress has not sanctioned a less rigorous code of conduct under the federal securities laws.

H.Rep. No. 355, 98th Cong., 2d Sess. 4-5 (1983) [hereinafter cited as ITSA House Report], *reprinted in* 1984 U.S.Code Cong. & Ad.News 2274, 2277-78 (footnotes omitted and emphasis added). Although Congress, in the ITSA, increased the sanctions available for insider trading violations, it did not attempt to provide a definition of insider trading because — once again expressly

citing the Second Circuit's decision in *United States v. Newman*, *supra* — "[t]he Committee believes that the law with respect to insider trading is sufficiently well-developed at this time to provide adequate guidance." *Id.* at 13, *reprinted in* 1984 U.S.Code Cong. & Ad.News at 2286.

Frequently, the misappropriation theory will hold liable those persons breaching a duty of trust and confidentiality to a tender offeror. Indeed, insiders of a tender offeror, because they are often the only ones with advance knowledge of an impending hostile tender offer, are the ones most likely to trade (or tip) on non-public information regarding a hostile tender.

The problem of insider trading on tender offers has become particularly acute, especially in conjunction with the greater availability of option contracts. Persons with advance knowledge of a tender offer announcement have opportunities to profit substantially in a short time with little or no risk of loss. These opportunities can be greatly maximized on the options market because the value of an option contract tends to increase by a much greater percentage than the value of the underlying stock.

By enacting the ITSA, Congress has expressed its heightened concern over the growing problem of insider trading. One of the ITSA's provisions is an amendment to section 21(d) of the Exchange Act, expanding the SEC's enforcement remedies; it gives SEC the authority to seek from anyone violating the insider trading laws a civil penalty of up to three times the amount of the profit gained (or loss avoided) by the insider trading.⁴³

Against the background of this analytic framework and heightened Congressional concern, we turn to the liability of the individual defendants in this case.

⁴³ Since this penalty provision was enacted after the St. Joe purchases at issue here, it is not applicable to this case. The SEC has not argued that this penalty provision should be applied retroactively.

III. LIABILITY

A. *Tome's Liability*⁴⁴

1. *Violation of Section 10(b) and Rule 10b-5*

In order to prove its civil claim against Tome for violation of Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b) (1982), and Rule 10b-5 promulgated thereunder, 17 C.F.R. 240.10b-5 (1985), the SEC must establish by a preponderance of the evidence,⁴⁵ (1) a misrepresentation, or an omission (where there is a duty to speak), or other fraudulent device; (2) in connection with the purchase or sale of any security; (3) scienter by the defendant in making that misrepresentation or omission, *Aaron v. SEC*, 446 U.S. 680, 691, 100 S.Ct. 1945, 1952, 64 L.Ed.2d 611 (1980); and

⁴⁴ The "fugitive from justice" rule limits a fugitive litigant's access to the courts for proceedings, both civil and criminal, related to the criminal proceedings in which he has refused to appear. *United States v. \$45,940 In United States Currency*, 739 F.2d 792, 798 (2d Cir.1984); see also *United States v. Sharpe*, 470 U.S. 675, 105 S.Ct. 1568, 1573 n. 2, 84 L.Ed.2d 605 (1985); *Molinaro v. New Jersey*, 396 U.S. 365, 90 S.Ct. 498 24 L.Ed.2d 586 (1970) (per curiam); *Conforte v. Commissioner*, 459 U.S. 1309, 1312, 103 S.Ct. 663, 664, 74 L.Ed.2d 588 (1983) (Rehnquist, J., in chambers). Since Tome's liability under the securities laws and regulations is clear, however, it is unnecessary to decide whether his "constructive flight", see *United States v. Catino*, 735 F.2d 718, 722 (2d Cir.), cert. denied, — U.S. —, 105 S.Ct. 180, 83 L.Ed.2d 114 (1984), from the related criminal proceeding, S 84 Cr. 534 (S.D.N.Y. filed August 7, 1984) affects his standing to defend this civil action. See *United States v. Baccollo*, 725 F.2d 170, 172 (2d Cir.1983). This issue, however, may gain added significance on appeal since Tome then will be attempting to invoke the jurisdiction of the appellate court.

⁴⁵ The preponderance of the evidence standard is the proper burden of proof both in injunctive actions brought by the SEC, see *Herman & MacLean v. Huddleston*, 459 U.S. 375, 390, 103 S.Ct. 683, 691-92, 74 L.Ed.2d 548 (1983) (action by private litigants to establish fraud under Section 10(b) of the Securities Exchange Act of 1934); *SEC v. C.M. Joiner Leasing Corp.*, 320 U.S. 344, 355, 64 S.Ct. 120, 125, 88 L.Ed. 88 (1934) (action by the SEC to establish fraud under Section 17(a) of the Securities Act of 1933); *SEC v. Commonwealth Chemical Securities, Inc.*, 574 F.2d 90, 102 (2d Cir.1978) (Friendly, J.), and in administrative proceedings before the SEC. *Steadman v. SEC*, 450 U.S. 91, 95, 101 S.Ct. 999, 1004, 67 L.Ed.2d 69 (1981).

(4) materiality of that misrepresentation or omission. See *Angelastro v. Prudential-Bache Securities, Inc.*, 764 F.2d 939, 942 & n. 5 (3d Cir.), *cert. denied*, — U.S. —, 106 S.Ct. 267, 88 L.Ed.2d 274 (1985); *Warren v. Reserve Fund, Inc.*, 728 F.2d 741, 744 (5th Cir.1984); *SEC v. Washington County Utility District*, 676 F.2d 218, 225 (6th Cir.1982). See generally *ABA Report, supra*, 41 *Bus.Law.* at 231.⁴⁶

a. *Misrepresentation, Omission, or Other Fraudulent Device*

Tome is liable under the misappropriation theory for the St. Joe purchases directly ordered by him for his NICO, TFCO, and Finvest Panama accounts at EBSI since he "fail[ed] to disclose material nonpublic information before trading on it and thus ma[de] 'secret profits.'"⁴⁷ *Dirks v. SEC*, 463 U.S. 646, 654, 103 S.Ct. 3255, 3261, 77 L.Ed.2d 911 (1983). He is also jointly and severally liable, with his tippees, for the St. Joe purchases of those he tipped since he improperly disclosed confidential corporate information to the tippees in breach of fiduciary or similar duty of trust and confidence to Seagram, its shareholders, and Bronfman.

At the time he bought St. Joe securities and tipped others to do likewise, Tome was an insider of Seagram, the tender offeror. Bronfman and Seagram reposed their trust and confidence in Tome's integrity; Tome callously and willfully betrayed that trust.

For many months, Bronfman had provided Tome with detailed (and continually updated) nonpublic information concerning

⁴⁶ Private litigants asserting a cause of action under Rule 10b-5 have the additional burden of providing (5) justifiable reliance upon the plaintiff's fraudulent device; and (6) damages resulting from the fraudulent device. In an SEC enforcement action, however, proof of these additional elements is not required.

⁴⁷ This Opinion need go no further than enforcement of the duty not to trade without disclosure to the beneficiary of the fiduciary relationship. *But see Carpenter, supra*, at 1034 ("because of [defendant Winan's] duty of confidentiality to the [Wall Street] Journal, [all] defendant[s] ... had a corollary duty, which they breached ... to abstain from trading in securities on the basis of the misappropriated information or to do so only upon making adequate disclosure to those with whom they traded.") (emphasis added).

Seagram's acquisition plans, solely for the confidential corporate purpose of evaluating Seagram's alternatives and gauging the European investment community's reaction to such a move.

The Supreme Court has recognized that persons, such as Tome here, given access to confidential corporate information solely for corporate purposes become temporary insiders of that corporation, thereby acquiring the same fiduciary duties to the corporation as other insiders:

Under certain circumstances, such as where corporate information is revealed legitimately to an underwriter, accountant, lawyer, or consultant working for the corporation, these outsiders may become fiduciaries of the shareholders. The basis for recognizing this fiduciary duty is not simply that such persons acquired nonpublic corporate information, but rather that they have entered into a special confidential relationship in the conduct of the business of the enterprise and are given access to information solely for corporate purposes.... When such a person breaches his fiduciary relationship, he may be treated more properly as a tipper than a tippee.... For such a duty to be imposed, however, the corporation must expect the outsider to keep the disclosed nonpublic information confidential, and the relationship at least must imply such a duty.

Dirks, 463 U.S. at 655 n. 14, 103 S.Ct. at 3262 n. 14.

Seagram and Bronfman of course expected their confidences to Tome to be kept confidential by him. The relationship between the management of a corporation and its financial advisors and consultants regarding prospective hostile tender offers is inherently one which implies a duty of confidentiality. Seagram and Bronfman certainly had such an expectation of confidentiality. As soon as Bronfman learned of this lawsuit and suspected that Tome's duty of confidentiality had been breached, Bronfman called Tome in Switzerland "to make doubly sure" Tome had not been involved in the illegal St. Joe purchases alleged in the SEC's complaint. Tome, on his part, explicitly acknowledged

his obligation to keep the information he received confidential when he lied to Bronfman about trading on the inside information he had. Had there been no expectation of confidentiality, there would have been no need for Tome to lie about his trading (and tipping) in St. Joe securities when Bronfman specifically questioned him.

Tome breached his fiduciary or similar duty of trust and confidence by trading for his own behalf in the St. Joe options purchased for his NICO, TFCO, and Finvest Panama accounts at BSI. He also breached his duty by tipping others, expecting in exchange both money (the \$200,000 he demanded Leati obtain from the benefitting customers of Lombardfin S.p.A.) and reputational benefits as a securities broker, that no doubt subsequently would result in increased business for him and his company, Finvest Geneva.

Tome, therefore, traded and tipped on the confidential inside information he received from Seagram and Bronfman about St. Joe, in breach of his fiduciary duty to Seagram, its shareholders, and Bronfman. He thereby committed fraud within the meaning of Section 10(b) and Rule 10b-5 by misappropriating valuable corporate information for his own benefit.

b. *In Connection With*

This requirement is easily satisfied since "[t]he information [Tome] stole ha[d] no value whatsoever except 'in connection with' his subsequent purchase of securities." *SEC v. Materia*, 745 F.2d 197, 203 (2d Cir.1984), *cert. denied*, — U.S. —, 105 S.Ct. 2112, 85 L.Ed.2d 477 (1985). The sole purpose of Tome's theft of confidential information regarding Seagram's tender offer plans "was to reap instant no-risk profits in the stock market." *Id.*; *see Newman*, 664 F.2d at 18.

c. *Scienter*

Although reckless deception satisfies the scienter requirement, *Sirota v. Solitron Devices, Inc.*, 673 F.2d 566, 575 (2d Cir.), *cert. denied*, 459 U.S. 838, 103 S.Ct. 86, 74 L.Ed.2d 80 (1982); *IIT*

v. Cornfeld, 619 F.2d 909, 923 (2d Cir.1980),⁴⁸ there is abundant evidence that Tome acted knowingly and intentionally in connection with his fraudulent activity. His frantic trading and tipping on march 10th and 11th, together with his eloquent silence concerning his frantic trading in St. Joe options when meeting Bronfman socially on the evening of March 11th—even though Bronfman was discussing with Tome the intimate details of the just-completed Seagram tender offer for St. Joe—and his subsequent lies when questioned specifically whether he had a beneficial interest in any St. Joe trades, all lead inescapably to the conclusion that Tome acted knowingly and intentionally in connection with his fraudulent activity. See *Elkind v. Liggett & Myers, Inc.*, 635 F.2d 156, 167 (2d Cir.1980) (“One who deliberately tips information which he knows to be material and non-public to an outsider who may reasonably be expected to use it to his advantage has the requisite scienter.”) (footnotes omitted).

d. *Materiality*

Tome clearly was in possession of material, nonpublic information when he breached his fiduciary or similar duty of trust and confidence to Seagram, its shareholders, and Bronfman by trading (and tipping). Information is material if there is a “substantial likelihood” that the information would be significant to a “reasonable investor” in making his or her investment decisions. *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 449, 96 S.Ct. 2126, 2132, 48 L.Ed.2d 757 (1976) (defining materiality under proxy regulation rule 14a-9); *Elkind*, 635 F.2d at 166 (applying the TSC standard to an action under Section 10(b) and Rule 10b-5, holding it to be “a relevant question in determining materiality ... whether the ... information ... would have been likely to affect the decision of potential buyers and sellers.”).

⁴⁸ The Supreme Court has not yet decided whether reckless deception satisfies the scienter requirement under Section 10(b) and Rule 10b-5. See *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193-94 n. 12, 96 S.Ct. 1375, 1381 n. 12, 47 L.Ed.2d 668 (1976). Since *Hochfelder*, however, ten different courts of appeals have either held or assumed that reckless deception is sufficient. See *ABA Report, supra*, 41 Bus.Law. at 241 n. 70 (collecting cases).

Through the myriad disclosures by Bronfman to Tome concerning Seagram's confidential tender offer plans and potential targets, and the information concerning the Seagram parent company's Montreal Board meeting, Tome knew that Seagram's tender offer for St. Joe was imminent. Knowledge of an impending tender offer that has not previously been announced publicly is clearly material information. *SEC v. Geon Industries, Inc.*, 531 F.2d 39, 47-48 (2d Cir.1976) (holding knowledge of a proposed merger to be material information in the context of an insider trading case). The significance of this information to investors is highlighted by the temporary halting of trading in St. Joe securities and by the virtually immediate jump in price of St. Joe stock from approximately \$30 per share to approximately \$45 per share when the Seagram tender offer was publicly announced on March 11. *See Elkind*, 635 F.2d at 166 (reaction of investors to the information is an indication of its materiality).

2. Violation of Section 14(e) and Rule 14e-3

The SEC argues that Tome (and the other defendants) also violated Section 14(e) and Rule 14e-3, 15 U.S.C. § 78n(e) and 17 C.F.R. § 240.14e-3, and that unlike a violation of Section 10(b) and Rule 10b-5, a violation of Rule 14e-3 does not require the SEC to prove scienter. *See Caleb & Co. v. E.I. DuPont de Nemours & Co.*, 599 F.Supp. 1468, 1472-73 (S.D.N.Y.1984) (holding that a violation of Rule 14e-1(c) does not require proof of scienter); *Caleb & Co. v. E.I. DuPont de Nemours & Co.*, 615 F.Supp. 96, 99 (S.D.N.Y.1985) (same, expressly citing *Schreiber*, at 101); *cf. Schreiber v. Burlington Northern, Inc.*, — U.S. —, 105 S.Ct. 2458, 2464 n. 11, 86 L.Ed.2d 1 (1985) (stating that the SEC has "latitude to regulate nondeceptive activities" under Section 14(e)). *But cf. id.* at 2646 (stating that Section 14(e) is "modeled on the antifraud provisions" of Section 10(b) and Rule 10b-5). Since scienter is clearly present in this case, and since defendants' liability is clear under Section 10(b) and Rule 10b-5, it is unnecessary also to decide that defendants could be held liable without proof of scienter under Section 14(e) and Rule 14e-3. *See Materia*, 745 F.2d at 203 n. 5.

B. *The Panamanian Defendants' Liability*

The Panamanian defendants, NICO, TFCO, and Finvest Panama, in a joint post-trial memorandum with Tome, concede that "[t]here is no question but that Tome directed and controlled the transactions at issue as agent of the Panamanian corporations, and consequently, whatever information Tome utilized in causing the Panamanian defendants to engage in these transactions may properly be imputed to them." Defendants' (Tome, NICO, TFCO, Finvest Panama) Post-Trial Memorandum, at 53.

We need not decide whether secondary liability can be imposed in this case upon the Panamanian defendants as controlling person under Section 20(a), 15 U.S.C. § 78t(a),⁴⁹ since it is clear that common law agency concepts apply to violations of Section 10(b) and Rule 10b-5. *Armstrong v. McAlpin*, 699 F.2d 79, 92 (2d Cir.1983); *SEC v. Management Dynamics, Inc.*, 515 F.2d 801, 812 (2d Cir.1975); *but cf. id.* at 813 ("We need not decide today whether the entire corpus of agency law is to be imported into the securities acts for all purposes."). Indeed, "since a corporation can act only through its agents," *id.* at 812, a corporation is liable, as a principal, for the actions of its responsible officers and authorized agents. *A.J. White & Co. v. SEC*, 556 F.2d 619, 624 (1st Cir.), *cert. denied*, 434 U.S. 969, 98 S.Ct. 516, 54 L.Ed.2d 457 (1977); *Verrechia v. Paine, Webber, Jackson & Curtis*, 563 F.Supp. 360, 364-65 (D.P.R.1982). Since, as defendants concede, Tome had actual authority to purchase the St. Joe options at issue here, under general agency principles, the Panamanian defendants are equally liable for Tome's violations of Section 10(b) and Rule 10b-5.

C. *Leati and Lombardfin S.p.A.'s Liability*

Although defendants Tome, NICO, TFCO, and Finvest Panama, through counsel, have appeared in this action, Leati,

⁴⁹ In order to establish secondary liability under Section 20(a), three elements must be proved: "(1) a primary violation, (2) scienter, and (3) control of the primary violator by the defendant." *Index Fund, Inc. v. Hagopian*, 609 F.Supp. 499, 511 (S.D.N.Y.1985).

Lombardfin S.p.A., and the Unknown Purchasers have not appeared.

Originally, when this suit was filed in March 1981, the SEC was not then able to determine exactly who had engaged in the trades complained of, only that the trades had taken place. To an extent, particularly with the Unknown Purchases, because of foreign secrecy laws, that problem still exists. When the SEC was able to determine exactly who was behind the trades, it amended the title of the suit, adding those additional defendants who had previously only been identified by category (*i.e.*, as "Unknown Purchasers"). At trial, on October 23, 1985, this Court, by default, granted plaintiff SEC's motion to amend the title of the lawsuit to add Leati and Lombardfin S.p.A. as defendants. Leati's testimony was taken in Italy in October 1985 pursuant to the Letter Rogatory procedure. Before then, the testimony of Csopey, which incriminates Leati as an active participant in this illegal trading activity, had been taken in New York in September 1985. Leati and Lombardfin S.p.A., therefore, clearly were aware of the pendency of this litigation but chose not to participate in it. In addition, after this suit was filed, in May 1982 the SEC effected personal service on all defendants pursuant to Rule 4, Federal Rules of Civil Procedure, by publication of a Summons with Notice of the pendency of this suit in newspapers of general circulation in Europe, including the *International Herald Tribune*. Leati read the *International Herald Tribune* in 1981.

Leati, as Tome's tippee, committed fraud within the meaning of Section 10(b) and Rule 10b-5 because, as the testimony of Csopey (admissible against Leati as a party admission) makes clear, Leati knew or should have known that Tome's disclosures to him were made in breach of Tome's fiduciary or similar duty of trust and confidence to Seagram, its shareholders, and Bronfman. *Dirks*, 463 U.S. at 660, 103 S.Ct. at 3264. Leati was a participant after the fact in Tome's fraudulent breach. *Id.* at 667, 103 S.Ct. at 3268; *Chiarella*, 445 U.S. at 230, 100 S.Ct. at 1115 n. 12. For the same reasons as were stated when discussing Tome's liability, the fraud was "in connection with" Leati's purchase of St. Joe securities and the information was clearly material. Finally, Csopey's testimony makes it clear beyond peradventure of

doubt that Leati had the requisite scienter, *i.e.*, that he intentionally and knowingly participated in this fraudulent scheme to trade on inside information. Although it appears that Leati did in fact have a beneficial interest in at least some of the accounts for which he purchased St. Joe securities, he need not necessarily have had a beneficial interest in the accounts in order to be held liable under these antifraud provisions. If in fact any personal benefit is necessary to hold tippees liable under Section 10(b) and Rule 10b-5,⁵⁰ the commissions and reputational benefits Leati expected to enjoy from this fraudulent scheme clearly suffice. Leati is liable to account for the illegal St. Joe trades in which he engaged.

Leati is Lombardfin S.p.A.'s founder, majority stockholder, vice-chairman of the Board of Directors, and general manager. In addition to an agency theory of liability, discussed previously in relation to the Panamanian defendants, the SEC urges that Lombardfin S.p.A. is liable for Leati's Section 10(b) and Rule 10b-5 violations under the doctrine of *respondent superior*. See *Marbury Management, Inc. v. Kohn*, 629 F.2d 705, 716 (2d Cir.) (holding the doctrine applicable to a 10b-5 claim against a broker trainee who had held himself out as a broker and had accounted to his employer for all buying and selling transactions in which he had engaged), *cert. denied sub nom.*, *Wood Walker & Co. v. Marbury Management Inc.*, 449 U.S. 1011, 101 S.Ct. 566, 66 L.Ed.2d 469 (1980); *Moss v. Morgan Stanley Inc.*, 553 F.Supp. 1347, 1356-57 (S.D.N.Y.) (holding the doctrine inapplicable to an insider trading case since the unauthorized trading was not within the scope of employment), *aff'd*, 719 F.2d 5 (2d Cir.1983), *cert. denied sub nom. Moss v. Newman*, 465 U.S. 1025, 104 S.Ct. 1280, 79 L.Ed.2d 684 (1984); *O'Connor*, 529 F.Supp. at 1194 (same).

⁵⁰ Since tippees are liable as participants after the fact in the insider's breach of his fiduciary or similar duty of trust and confidence—which breach requires some personal gain to the insider—and are therefore not required to have independently breached some duty, it is not clear that tippees must personally benefit from their trades or subsequent tips to others to be held liable under Section 10(b) and Rule 10b-5 (*e.g.*, a tippee who does not trade but who merely tips another who trades), although it appears likely that in a majority of cases some personal benefit to the tippee will be present.

But because of Leati's prominent position in Lombardfin S.p.A., it is not necessary to rely on the doctrine of *respondent superior* to hold Lombardfin S.p.A. liable. In the context of a Rule 10b-5 claim, the Third Circuit appositely held that:

high ranking officers in a corporation, or partners in a partnership, present a different situation from lower level employees. Officers are able to make policy and generally carry authority to bind the corporation. Their action in behalf of the corporation is therefore primary, and holding a corporation liable for their actions does not require respondeat superior.

Sharp v. Coopers & Lybrand, 649 F.2d 175, 182 n. 8 (3d Cir.1981), cert. denied, 455 U.S. 938, 102 S.Ct. 1427, 71 L.Ed.2d 648 (1982). Because of Leati's violations of Section 10(b) and Rule 10b-5, Lombardfin S.p.A. is jointly liable for Leati's trading in St. Joe securities.

D. BSI's Liability

Two million dollars and 1,200 shares of Fluor Corporation stock, plus dividends, are frozen in BSI's account at Irving Trust Company, in the City of New York, pursuant to this Court's previous orders. Shortly before Seagram announced a tender offer for St. Joe Mineral stock, BSI bought 1,055 call option contracts on the Philadelphia, Pennsylvania options market for its bank customers through an American stockbroker to acquire shares of St. Joe Minerals and purchased 3,000 shares of such stock. Shortly thereafter, it ordered the liquidation of the the call options for \$1,849,843.13, and the liquidation of 2,000 of the 3,000 shares for \$92,739.35. The proceeds wound up in the BSI account at Irving Trust Company, and were there when this Court froze the account on application of the SEC.

BSI balances at the Irving Trust Company at the close of business on March 27, 1981 consisted of cash deposits of not less than \$4,900,000, and United States marketable securities of a then-market value of not less than \$326,000,000. Irving Trust Company appeared before the Court and conceded that it was in the

position of a stakeholder of the proceeds of the trades in St. Joe Minerals. BSI appeared before the Court and stated its consent to an order providing for the temporary security in the amount of two million dollars *to cover* proceeds with respect to the questioned transactions, and thereupon requested the release of the balance of the BSI bank account. That consent and security "to cover" the avails of the trading was renewed from time to time, and continues to exist right down to date.

Efforts to disclose the alleged anonymous customers of the bank were thwarted for a substantial period, but ultimately it was established that the Panamanian defendants referred to above were the purchasers and sellers of the calls and the stock. BSI was represented before the Court in this action, its counsel stating, as early as June 12, 1981, "However, with respect to the \$2 million which we are prepared to consent to, we are clearly in that regard willing to allow this court *in rem* jurisdiction to the extent of that \$2 million. We have no difficulty in that regard." On the representation of BSI, it seemed to the Court that the amount frozen in the new York account seemed to be adequate "to cover" the liability asserted against the then-Unknown Purchasers, later identified as the Panamanian defendants.

During the course of the litigation, it was represented to the Court that Swiss authorities had frozen funds of Unknown Purchasers at its Lugano branch. Whether the Unknown Purchasers were only the Panamanian defendants, or purchasers in addition thereto, is not clear. To avoid any juggling of the accountability for the improper trading of the Panamanian defendants as between the Lugano branch and the frozen account of BSI in New York, the Court ordered the New York branch of BSI to request that any proceeds of St. Joe trading attributable to the Panamanian companies and frozen in the Lugano offices be transferred to the New York branch, and thereafter be paid into Court to be included in the avails, subject to the disgorgement directed hereafter.

Double-payment of the avails of the trading is not intended; only that BSI be required to turn over to the plaintiff two million

dollars "to cover" the proceeds for which the Panamanian defendants are accountable under the findings in this decision. Additionally, BSI is ordered to pay the 1,200 shares of Fluor Corporation, together with dividends accumulated thereon since March 1981, proceeds from the illegal St. Joe trades held by Irving Trust Company, into the Court forthwith. Until these events have occurred, the freeze on the two million dollars in BSI's account at Irving Trust Company remains in effect. The next section of this decision deals with Unknown Purchasers other than the Panamanian defendants.

E. Unknown Purchasers

The Court has been informed that the Government of Switzerland has frozen at least some Unknown Purchasers' accounts containing funds relating to the illegal St. Joe transactions discussed herein. The Court dismisses, and does not adjudicate, the claims of the SEC against the Unknown Purchasers, without prejudice to any subsequent action by the SEC to determine the identities of the Unknown Purchasers or to attempt to collect the Unknown Purchasers' profits from their unlawful St. Joe purchases. Additionally, the claims of the SEC not adjudicated herein are severed and discontinued, without prejudice, to the extent that it subsequently may be discovered that Tome, Leati, Lombardfin S.p.A., or the Panamanian defendants have a further beneficial interest in any funds or accounts of the Unknown Purchasers frozen by the Swiss Government or frozen in BSI's Lugano office or located in Guernsey.

F. Remedies

1. Disgorgement

Defendants Tome, NICO, TFCO, and Finvest Panama contend that even if they are found to have violated the securities laws and regulations, disgorgement of ill-gotten gains is an inappropriate remedy in actions brought under the misappropriation theory. These defendants argue that since private plaintiffs themselves could not sue to recover these defendants' illegal profits (because of judicially-created standing requirements for a private

cause of action under Rule 10b-5, *see supra* note 41), allowing the SEC to do so would constitute an unauthorized "penalty." In essence, these defendants argue that although they were caught violating the law and reaping millions of dollars in illegal profits in so doing, once caught they need not account to anyone for these illegal profits. Neither existing case law nor policy considerations supports such an inequitable result.

In a Second Circuit decision on the misappropriation theory, the court affirmed the district court's order of disgorgement of ill-gotten gains, noting that "[d]isgorgement of illegally obtained profits is by no means a new addition to this category of permissible equitable remedies [under Section 21(d)]." *Materia*, 745 F.2d at 201. And Congress, in enacting the enhanced penalties for insider trading under the ITSA, has recently underscored the importance of the disgorgement remedy in SEC injunctive actions:

The principal, and often effectively [the] only, remedy available to the Commission against insider trading is an injunction against further violations of the securities laws and disgorgement of illicit profits.

ITSA House Report, *supra*, at 7, *reprinted in* 1984 U.S. Code Cong. & AdNews at 2280. In enacting these increased sanctions, Congress expressed its belief that disgorgement of illegal profits was insufficient to deter insider trading:

Disgorgement of illegal profits has been criticized as an insufficient deterrent, because it merely restores a defendant to his original position without extracting a real penalty for his illegal behavior. The risk of incurring such penalties often fails to outweigh the temptation to convert nonpublic information into enormous profits.

Id. at 7-8, *reprinted in* 1984 U.S. Code Cong. & AdNews at 2280-81. If the Congress believes that even full disgorgement of profits is an insufficient deterrent to insider trading, *a fortiori* less than full disgorgement, or as the defendants argue, none, is even more ineffectual. Long ago, in the first court of appeals

decision ordering disgorgement in an SEC enforcement action, the Second Circuit recognized that those who trade on inside information are simply after quick, no-risk profits, and therefore that the most effective means to deter such behavior is to make the activity unprofitable. *Texas Gulf Sulphur*, 446 F.2d at 1308 ("It would severely defeat the purposes of the [Exchange] Act if a violator of Rule 10b-5 were allowed to retain the profits from his violation."); see also *CFTC v. British American Commodity Options Corp.*, 788 F.2d 92, 94 (2d Cir. 1986) ("disgorgement serves the purpose of depriving the wrongdoer of his ill-gotten gains and deterring violations of law."); *SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1104 (2d Cir.1972) ("The effective enforcement of the federal securities laws requires that the SEC be able to make violations unprofitable.").

At bottom, the defendants' arguments rest on the proposition that the SEC stands in the shoes of private litigants in bringing this injunctive proceeding. Such an assertion, however, was affirmatively rejected in *SEC v. Petrofunds, Inc.*, 420 F.Supp. 958, 960 (S.D.N.Y.1976):

[There is a] critical distinction between actions brought by the SEC and actions brought by private litigants. Regardless of the fact that defendants may be required to disgorge profits, the SEC in no way stands in the shoes of a private litigant with respect to its claims for ancillary relief.

See also *Management Dynamics*, 515 F.2d at 808 ("the SEC appears in these proceedings not as an ordinary litigant, but as a statutory guardian charged with safeguarding the public interest in enforcing the securities laws."). Disgorgement, therefore, is an appropriate, indeed an essential, remedy in an SEC enforcement action based on a misappropriation theory of insider trading liability.

The defendants found liable herein shall account for and disgorge all profits and dividends received or credited, plus interest at the average prime rate from March 11, 1981 to the date of this Opinion, from any purchases of St. Joe stock or options

between February and March 11, 1981. Defendant Tome is liable (1) individually, for accounts in which he held any economic, beneficial, or discretionary interest, and (2) jointly and severally with his tippees, the Panamanian defendants (NICO, TFCO, Finvest Panama), Leati, and Lombardfin S.p.A., for accounts in which those tippees, direct and secondary, held any economic, beneficial, or discretionary interest. Without limiting the scope of liability, Tome is liable for all profits and dividends plus interest, from all St. Joe stock and option purchases discussed in this Opinion. Tome's liability is joint and several with that of the Panamanian defendants for the St. Joe options purchased for the NICO, TFCO, and Finvest Panama accounts at BSI, and with Leati and Lombardfin S.p.A. for the St. Joe stock and option purchases placed by Leati or his subordinates for Lombardfin S.p.A.'s clients. These defendants are ordered to pay these amounts into the Court to be included in the amount subject to disgorgement. The decree to be submitted herein should set forth a plan for disgorgement and administration of the fund to be created, taking due account of similar plans previously utilized in like decisions.

2. *Permanent Injunction*

Once the SEC has proven a defendant's violation of the securities laws and regulations, it makes a "proper showing" for permanent injunctive relief, within the meaning of Section 21(d), by demonstrating, by a preponderance of the evidence, a "reasonable likelihood that the wrong will be repeated." *Manor Nursing Centers*, 458 F.2d at 1100-01; *see also Management Dynamics*, 515 F.2d at 807. In determining whether a permanent injunction is appropriate, a "district court is called upon to assess all those considerations of fairness that have been the traditional concern of equity courts." *Manor Nursing Centers*, 458 F.2d at 1102; *see also Management Dynamics*, 515 F.2d at 807 ("Whether the inference that the defendant is likely to repeat the wrong is properly drawn, however, depends on the totality of the circumstances . . ."); *see also SEC v. Monarch Fund*, 608 F.2d 938, 943 (2d Cir.1979); *SEC v. Commonwealth Chemical Securities, Inc.*, 574 F.2d 90, 99 (2d Cir.1978); *SEC v. Bausch*

✓ *Lomb, Inc.*, 565 F.2d 8, 18 (2d Cir.1977); *CFTC v. U.S. Metals Depositary Co.*, 468 F.Supp. 1149, 1161-62 (S.D.N.Y. 1979). The Second Circuit has provided additional guidance by enumerating specific factors the court should consider in making this determination:

The factors which [a district judge] may consider include the likelihood of future violations, the degree of scienter involved, the sincerity of defendant's assurances against future violations, the isolated or recurrent nature of the infraction, defendant's recognition of the wrongful nature of his conduct, and the likelihood, because of defendant's professional occupation, that future violations might occur.

SEC v. Universal Major Industries Corp., 546 F.2d 1044, 1048 (2d Cir.1976), *cert. denied sub nom.*, *Homans v. SEC*, 434 U.S. 834, 98 S.Ct. 120, 54 L.Ed.2d 95 (1977).

Applying these factors to this case, it is clear that the SEC is entitled to injunctive relief against defendants Tome, the Panamanian defendants, Leati, and Lombardfin S.p.A. and this court so orders. Tome acted intentionally in deceiving Bronfman and Seagram, abusing his position of trust and confidence, eventually lying about his activities when questioned specifically. *SEC v. Aaron*, 605 F.2d 612, 624 (2d Cir.1979) ("the [district] court's finding that appellant acted with scienter underscore[s] the need for an injunction."), *vacated on other grounds*, 446 U.S. 680, 100 S.Ct. 1945, 64 L.Ed.2d 611 (1980). Tome not only traded for himself, but tipped others to encourage them to engage in illegal conduct. In fact, the evidence indicates that, before the St. Joe trades forming the basis of this suit, Tome had engaged in other trades on inside information confidentially disclosed by Bronfman concerning Seagram's tender offer plans. Tome has not indicated any remorse for his actions, except in being caught. He has remained outside the United States to avoid prosecution on a related criminal charge. In addition, his position as a broker and financial advisor would enable him to violate the law again.

The Panamanian defendants have not admitted their complicity in this scheme either. Tome has a beneficial interest in these

accounts, and had discretionary power over them. Finvest Panama is part of Tome's Finvest Group, his financial network. Should Tome attempt to violate the law again, it appears likely that he would attempt to use these corporate entities to do so.

Leati acted intentionally in engaging in the St. Joe trades on the basis of Tome's inside information. Indeed, there is evidence in the record that Leati previously traded on Tome's inside information. He has expressed no remorse for what he did; in fact, he has refused to appear in this action. His position as a broker and financial advisor would enable him to violate the law again.

As discussed previously, Lombardfin S.p.A. is dominated by Leati, both as owner and as manager. Csopey testified that other high-ranking officials of Lombardfin S.p.A. knew about the illegal trading shortly after its occurrence but did nothing to rectify the situation. Should Leati attempt to violate the law again, it appears likely that he would attempt to use Lombardfin S.p.A. to do so.

For these reasons, Tome, NICO, TFCO, Finvest Panama, Leati, and Lombardfin S.p.A. are permanently enjoined from violating the antifraud provisions of the United States securities laws and regulations.

The foregoing shall constitute the findings of fact and conclusions of law required under Rule 52(a), Federal Rules of Civil Procedure. A decree in separate form, without reciting the prior proceedings, *see* Rule 54, should be submitted on ten (10) days notice, within thirty (30) days hereof.

So Ordered.

SECURITIES AND EXCHANGE COMMISSION, Plaintiff,

v.

Giuseppe B. TOME, Paolo Mario Leati, Lombardfin S.p.A., Transatlantic Financial Co., S.A., Nayarit Investments, S.A., Finvest Underwriters and Dealers Corp., Certain Purchasers of the Common Stock and Call Options for the Common Stock of St. Joe Minerals Corp., and Banca Della Svizzera Italiana, Defendants.

No. 31 Civ. 1836 (MP).

United States District Court,
S.D. New York.

June 3, 1986.

Ira Lee Sorkin, Regional Adm'r, S.E.C. by Anne C. Flannery, Robert B. Blackburn, Joseph G. Mari, Philip M. Giordano, Jennifer M. Russell, New York City, for plaintiff.

John F.X. Peloso, Daniel B. McIntyre, Sage Gray Todd & Sims, New York City, for defendant Giuseppe B. Tome.

Bruno Schachner, New York City, for defendants Transatlantic Financial Co., S.A., Nayarit Investments, S.A., Finvest Underwriters and Dealers Corp.

Chester J. Straub, David Trachtenberg, Wilkie Farr and Gallagher, New York City, for defendant Banca Della Svizzera Italiana.

MEMORANDUM

MILTON POLLACK, Senior District Judge.

Evidentiary Rulings

During the course of the non-jury trial herein, motions were presented by the parties for evidentiary rulings on which decision was reserved. The questions raised by the parties relate to the effect to be given to defendant Tome's assertion of his

Fifth Amendment privilege against self-incrimination and to the admissibility of portions of depositions and other exhibits submitted as evidence.

A. The Effect of Tome's Assertion of His Fifth Amendment Privilege Against Self-Incrimination

The plaintiff SEC sought to obtain responses from defendant Tome to interrogatories to be addressed to him in Switzerland. In an affidavit, Tome asserted his Fifth Amendment privilege against self-incrimination and refused to answer any interrogatories related to the transactions at issue in this case. Tome contends, however, that it is constitutionally impermissible for this Court to draw an adverse inference from that assertion of the privilege. Implicitly conceding that an adverse inference may be drawn in a civil case between private parties, Tome contends that it is constitutionally impermissible for this Court to do so in a civil case in which the government is the plaintiff or in which the defendant invoking the privilege is also a defendant in a parallel criminal proceeding. He relies upon language in a dissent in *Baxter v. Palmigiano*, 425 U.S. 308, 334, 96 S.Ct. 1551, 47 L.Ed.2d 810 (1976) (Brennan, J. dissenting) and some glancing dicta in *SEC v. Musella*, 578 F.Supp. 425, 431 (S.D.N.Y.1984). Tome's contention is contrary to the settled law. See *United States v. Segal*, 549 F.2d 1293, 1299 (9th Cir.), (*Baxter* "held that a negative, though not conclusive, inference can be drawn from the failure of a prisoner to testify . . . even though the testimony if given could lead to criminal prosecution."), *cert. denied*, 431 U.S. 919, 97 S.Ct. 2187, 53 L.Ed.2d 231 (1977).

The authorities cited below would have fully justified drawing an adverse inference against Tome from his assertion of the privilege against self-incrimination herein. In the circumstances presented, however, it is unnecessary to utilize the inference to establish liability. Even if needed to establish liability, it would have been merely one inference among a number of evidentiary factors considered by this Court in reaching its conclusions. Tome's liability herein has been established by a preponderance of the credible evidence, without regard to the adverse inference.

Baxter, supra, established that the Constitution does not prohibit drawing an adverse inference from a party's assertion of the privilege in civil cases since "silence in the face of accusation is a relevant fact. . . . [and] 'is often evidence of the most persuasive character.'" *Baxter*, 425 U.S. at 319, 96 S.Ct. at 1558 (quoting *United States ex rel. Bilokumsky v. Tod*, 263 U.S. 149, 153-54, 44 S.Ct. 54, 56, 68 L.Ed.2d 221 (1923) (Brandeis, J.)). The next year, in *Lefkowitz v. Cunningham*, 431 U.S. 801, 808 n. 5, 97 S.Ct. 2132, 2137 n. 5, 53 L.Ed.2d 1 (1977), the Supreme Court read its *Baxter* decision to mean that:

Baxter did no more than permit an inference to be drawn in a civil case from a party's refusal to testify. Respondent's silence in *Baxter* was only one of a number of factors to be considered by the finder of fact in assessing a penalty, and was given no more probative value than the facts of the case warranted[.]

The Second Circuit has interpreted the *Baxter* rule to apply to witnesses as well as parties and through these witnesses, former employees of a party, against a party. *Brink's Inc. v. City of New York*, 717 F.2d 700, 708-10 (2d Cir.1983).

Subsequent to *Baxter* and *Lefkowitz, supra*, decisions by federal courts have established that an adverse inference is equally to be drawn where the government is a party to the civil proceeding. *see e.g. FTC v. Kitco of Nevada, Inc.*, 612 F.Supp. 1282, 1291 (D.Minn.1985) (adverse inference drawn in an FTC enforcement action); *United States v. Local 560, International Brotherhood of Teamsters*, 581 F.Supp. 279, 306 (D.N.J.1984) (adverse inference drawn in civil RICO case brought by the government), *rev'd as to this point on other grounds*, 780 F.2d 267, 292-93 n.32 (3d Cir.1985); *CFTC v. U.S. Metals Depositary Co.*, 468 F. Supp. 1149, 1162 & n. 56 (S.D.N.Y.1979). Particularly relevant hereto, courts have drawn an adverse inference in enforcement actions brought by the SEC. *See e.g. SEC v. Netelkos*, 592 F.Supp. 906, 917-18 (S.D.N.Y.1984); *SEC v. Musella*, 578 F.Supp. 425, 429-30 (S.D.N.Y.1984); *SEC v. Scott*, 565 F.Supp. 1513, 1533-34 (S.D.N.Y.1983), *aff'd sub nom, SEC v. Cayman Islands Reinsurance Corp.*, 734 F.2d 118 (2d Cir.1984); *SEC v. Gilbert*, 79

F.R.D. 683, 686 (S.D.N.Y.1978). In addition, federal courts have held that the pendency of related criminal proceedings is irrelevant in determining whether to draw an adverse inference, *see e.g., Diebold v. Civil Service Commission*, 611 F.2d 697, 701 (8th Cir.1979) (holding that the fact that the defendant asserting the privilege in a civil action has already been indicted "has no bearing on the constitutional issues involved"); *Roberts v. Taylor*, 540 F.2d 540, 542 (1st Cir. 1976) (stating that the *Baxter* decision does not "accord leeway" for distinctions between a situation in which criminal charges are pending and a situation in which only a possibility of criminal charges are involved), *cert. denied sub nom., Roberts v. Director, Department of Corrections*, 429 U.S. 1076, 97 S.Ct. 819, 50 L.Ed.2d 796 (1977), and many decisions have drawn an adverse inference when criminal charges are pending. *See e.g. Hoover v. Knight*, 678 F.2d 578, 582 & n. 1 (5th Cir.1982); *Book v. United States Postal Service*, 675 F.2d 158, 160 n.4 (8th Cir. 1982) (per curiam); *Arthurs v. Stern*, 560 F.2d 477, 478 (1st Cir.1977), *cert. denied*, 434 U.S. 1034, 98 S.Ct. 768, 54 L.Ed.2d 782 (1978); *Rhode Island v. Cardillo*, 592 F.Supp. 655, 658 (D.R.I.1984); *Marcello v. Long Island Railroad*, 465 F.Supp. 54, 61 (S.D.N.Y.1979).

The permissible adverse inference has been used, however, only for the purpose of determining the *scope* of Tome's liability, following a determination of his liability without use of that inference. It is used herein only for some of the transactions engaged in by those whom Tome tipped regarding the Seagram tender offer for St. Joe, specifically the transactions engaged in by Banque Gutzwiller and by Trade Development Bank.

B. Objections To Testimony and Exhibits

Except for two live witnesses testifying at trial, Marc Cohen, an analyst in mining industries for the brokerage firm of Kidder, Peabody & Co., and Kevin Feehan, the New York Stock Exchange specialist in St. Joe stock, all testimony in this case was received by deposition testimony. All parties appearing in this action stipulated that the deposition testimony would be admissible as though that person were testifying live at trial, and thus

absence from the trial poses no hearsay objection because of that absence.

The testimony of some foreign nationals, Mrs. Patricia Arbucias, Mr. Riccardo Argenziano, and defendant Leati, all officers and/or directors of defendant Lombardfin S.p.A., was taken pursuant to a special Letter Rogatory procedure. The range of questions permitted in such proceedings is much narrower than the range permitted in our deposition procedure; thus the information obtained is much less complete.

After giving the parties an opportunity to object on the grounds of competency, relevancy, or hearsay, to the receipt by the Court of any portions of any of the deposition testimony, defendant Tome, joined by defendants NICO, TFCO, and Finvest Panama, objected to three isolated statements in Bronfman's deposition and to Csopey's deposition testimony to the extent that he repeated what Leati told him that Tome had said in telephone conversations between Leati and Tome on March 10, 1981. All other possible objections to the deposition testimony are waived.

In addition, both plaintiff and defendants objected to documents offered into evidence as exhibits. The SEC's objections are overruled and all of defendants' exhibits, including those offered after the trial on October 23, 1985, are received into evidence. The defendants' objections to the SEC's exhibits are sustained in part, overruled in part as discussed below in more detail.

1. Defendants' Hearsay Objections To Csopey's Testimony

Defendants object to Csopey's testimony on hearsay grounds to the extent that he testified concerning what his partner Leati had told him about business telephone conversations between Tome and Leati on March 10, 1981. Csopey was an interested party in the business. The SEC asserts that this contested testimony is not hearsay since it is "a statement by a coconspirator of a party during the course and in furtherance of the conspiracy." Rule 801(d)(2)(E), Fed.R.Evid. The SEC claims that since Leati was Tome's coconspirator in the illegal St. Joe purchases, Leati's statements to Csopey are admissible against Tome since they were

made during the course of and in furtherance of the conspiracy. In the alternative, the SEC argues that even if the contested statements are hearsay, several exceptions to the hearsay rule are applicable. Since the coconspirator exclusion from hearsay, Rule 801(d)(2)(E), by itself permits receipt of the matter objected to, it is unnecessary to discuss the SEC's other grounds for admitting the contested testimony.

Although the vast majority of cases discussing the coconspirator exclusion from the hearsay rule are criminal cases, *see generally* Annot., *Admissibility of Statement By Coconspirator Under Rule 801(d)(2)(E) of Federal Rules of Evidence*, 44 A.L.R.Fed. 627 (1979) (collecting cases), it is clear that the rule is equally applicable to civil cases. Rule 1101(b), Fed.R.Evid.; *see e.g. Filco v. Amana Refrigeration, Inc.*, 709 F.2d 1257, 1267 (9th Cir.) (discussing coconspirator exclusion in a civil case), *cert. dismissed*, 464 U.S. 956, 104 S.Ct. 385, 78 L.Ed.2d 331 (1983); *Oreck Corp. v. Whirlpool Corp.*, 639 F.2d 75, 80-81 (2d Cir.1980) (same), *cert. denied*, 454 U.S. 1083, 102 S.Ct. 639, 70 L.Ed.2d 618 (1981). There is a paucity of civil cases involving the coconspirator exclusion, however, and it is not clear whether the same principles applicable to its use in the criminal area are equally applicable in the civil area. *See generally* Note, *Reconciling The Conflict Between The Coconspirator Exemption From The Hearsay Rule and The Confrontation Clause of The Sixth Amendment*, 35 Colum.L.,Rev. 1294 (1985) (discussing possible Confrontation Clause problems on the criminal side). *But see United States v. Inadi*, — U.S. —, 106 S.Ct. 1121, 89 L.Ed.2d 390 (1986) (holding that the Confrontation Clause does not require a showing that the declarant is unavailable as a condition to admission of out-of-court statements by a nontestifying coconspirator).¹ In addition, the coconspirator exemption, in

¹ The *Inadi* opinion did not purport to address another possible Confrontation Clause concern noted by commentators, *i.e.*, whether the coconspirator's statements must be shown to be independently reliable before being admitted. *Inadi*, 106 S.Ct. at 1124 n. 3 ("The reliability of the out-of-court statements is not at issue in this case.") Compare *United States v. Perez*, 702 F.2d 33, 37 (2d Cir.) (indicating that an independent reliability determination must be made

(Footnote continued)

effect, would be rendered a nullity on the civil side if courts required the same quantum of proof in civil actions that is presently applicable in criminal actions, *i.e.*, the preponderance of the evidence standard, *see United States v. Ciambrone*, 787 F.2d 799, 807 (2d Cir.1986); *United States v. Geaney*, 417 F.2d 1116, 1120 (2d Cir.1969), *cert. denied sub nom.*, *Lynch v. United States*, 397 U.S. 1028, 90 S.Ct. 1276, 25 L.Ed.2d 539 (1970), before the conspirator's statement is admissible. Were a party to a civil action required to prove the existence of the conspiracy by a preponderance of the nonhearsay evidence before the coconspirator's statement is admissible, the coconspirator's statement would be merely corroborative evidence tending to reinforce the case already proved.² Perhaps this insight explains the dearth of civil cases addressing the coconspirator exclusion from the hearsay rule.

In this case, however, it is unnecessary to determine whether the predicate for admission of the coconspirator's statement is lower on the civil than on the criminal side since the SEC has proved the existence of a conspiracy by a preponderance of the independent evidence, *i.e.*, by admissible evidence other than the contested coconspirator's statements.³ The contested testimony

but stating that a declaration in furtherance of the conspiracy will often be sufficient to demonstrate reliability), *cert. denied*, 462 U.S. 1108, 103 S.Ct. 2457, 77 L.Ed.2d 1336 (1983) *with United States v. Aboumoussallem*, 726 F.2d 906, 910 (2d Cir.1984) ("*Even if we were to require some indicia of reliability beyond the circumstance of a co-conspirator's making a report that futhers a conspiracy ...*") (emphasis added). Whatever the eventual resolution of this Confrontation Clause concern may be for criminal cases, in a civil case, where Confrontation Clause concerns are not present, no independent reliability determination is required.

² This dilemma does not occur in criminal cases because of the difference in the quantum of proof necessary for conviction, *i.e.*, proof beyond a reasonable doubt, and for admission of the coconspirator's statement, *i.e.*, preponderance of the evidence.

³ Of course, had the independent evidence of the conspiracy not met the preponderance standard, this Court could use the adverse inference drawn from Tome's assertion of his Fifth Amendment privilege as a factor to consider on the SEC's burden of proof as to the conspiracy's existence and as to the conspiracy's participants.

of Csopey merely reinforces the credibility of circumstantial evidence already sufficient to hold defendants liable.

It is not necessary to charge a conspiracy in the complaint in order to invoke the coconspirator exclusion from the hearsay rule. *United States v. Doulin*, 538 F.2d 466, 471 (2d Cir.), *cert. denied*, 429 U.S. 895, 97 S.Ct. 256, 50 L.Ed.2d 178 (1976); *see United States v. Clark*, 613 F.2d 391, 402-04 (2d Cir.1979) (even if acquitted on the conspiracy count, coconspirator's statements may be admissible on the substantive count), *cert. denied*, 449 U.S. 820, 101 S.Ct. 78, 66 L.Ed.2d 22 (1980). Charging a substantive violation is sufficient. *United States v. Branker*, 418 F.2d 378, 380 (2d Cir.1969). When conspiracy is not charged, however, participants in the conspiracy often are referred to instead as "joint venturers," *see Clark*, at 404, or as "acting in concert," *see* 4 J. Weinstein & M. Berger, *Weinstein's Evidence* ¶ 801(d)(2)(E)[01] at 801-230 & n. 5 (1985), and that language appears to be apposite herein.

In determining whether the prosecution has proved by a preponderance of the evidence the existence of a "joint venture" and the defendants' participation in it, "pieces of evidence must be viewed not in isolation but in conjunction." *Geaney*, 417 F.2d at 1121. Further, " 'each of the episodes gain[s] color from each of the others.' " *United States v. Sliker*, 751 F.2d 477, 494 (2d Cir.1984) (quoting *United States v. Monia*, 295 F.2d 400, 401 (2d Cir.1961), *cert. denied*, 368 U.S. 953, 82 S.Ct. 395, 7 L.Ed.2d 386 (1962)), *cert. denied sub nom.*, *Buchwald v. United States*, — U.S. —, 105 S.Ct. 1772, 84 L.Ed.2d 832 (1985).

Unquestionably, Tome and Leati were engaged in a joint venture to illegally trade on inside information concerning Seagram's unannounced bid for control of St. Joe. Without regard to the contested portions of Csopey's testimony, the evidence—particularly Bronfman's testimony, the BSI employees' affidavits, and Tome's trading activity—convincingly demonstrates that Tome misappropriated confidential non-public information regarding Seagram's acquisition plans and traded on it for his own benefit.

Tome also engaged in a joint venture with Leati to exploit this nonpublic information that Tome possessed. The personal

relationship between Tome and Leati and, consequently, the close business relationship between Finvest Geneva and Lombardfin S.p.A. provided fertile ground for this illicit conduct. Leati had known Tome for years, even before Leati went into brokerage. As detailed in the accompanying Opinion in this case, at 8-9, because of this personal relationship, Tome's Finvest Group, particularly Finvest Geneva, had close business ties to Lombardfin S.p.A.; Lombardfin S.p.A.'s two principal foreign affiliates were renting their *only* office space, if it could be called that, from Finvest Geneva; Tome regularly visited Lombardfin S.p.A.'s domestic subsidiary's offices and used its facilities to conduct his business; a 100 % owned Lombardfin S.p.A. affiliate executed Eurobond trades on Finvest Geneva's behalf because Finvest Geneva did not have the capacity to clear trades; Finvest Geneva had a securities trading account with a 100 % owned Lombardfin S.p.A. affiliate.

Against this backdrop of interaction and familiarity, the joint venture flowered. After his telephone conversation with Bronfman on March 9, Tome on March 10 began his frantic trading and tipping to overseas clients and associates.*

By the end of the day, Leati, acting on his discretionary authority, had purchased for Lombardfin S.p.A.'s clients, over 40,000 St. Joe shares, despite the fact that before March 10, 1981, Lombardfin S.p.A. had not traded even one single share of St. Joe stock. Leati's futile attempt to justify such enormous trading on a stock he had never previously traded, with Leati's trading beginning *two minutes* after speaking to Tome, by claiming that he engaged in some sort of independent analysis of the stock only adds an additional inference to the already overwhelming circumstantial evidence that Tome and Leati were engaged in an illicit joint venture to profit from the inside information Tome possessed concerning Seagram's plans to make a tender offer for St. Joe.

* Tome's hotel only registered outgoing calls, and took messages if Tome was not in; no hotel records are kept of incoming calls if Tome was in to receive the call or if no message was left.

The statements Leati made to Csopey concerning the contents of Leati's conversations with Tome were made during the course of and in furtherance of the joint venture. Leati spoke to Csopey, Leati's partner in and co-founder of Lombardfin S.p.A., privately, in Leati's office, on the afternoon of March 10th, after speaking to Tome on the phone. While the outer temporal boundaries of a conspiracy's existence are often subject to debate, this conversation between Leati and Csopey took place right after this newly-formed illicit joint venture between Tome and Leati. Unquestionably, the contested statements took place during the course of the conspiracy. Leati made additional purchases of St. Joe securities for Lombardfin S.p.A.'s clients after the conversation with Csopey. Given the evidence in this case, it appears that the illicit association continued at least through the time that Tome was anticipating the recompense of \$200,000 mentioned by Csopey (but denied by Leati) for the inside information Tome supplied to Leati for Lombardfin S.p.A.'s clients.

The statements Leati made to Csopey were also in furtherance of the illicit venture; they were intended to bring Leati's partner (who owned 12.5% of Lombardfin S.p.A.'s stock) up-to-date on the significant news that had occurred while Csopey was out in the field visiting clients and to solicit his partner's ratification of the prior St. Joe transactions and approval for further purchases. After recounting the discussions between himself and Tome, and discussing the possible accuracy of Tome's information in light of Tome's confidential position as a Seagram advisor, Leati suggested even further purchases of St. Joe securities, saying "Let's give it a try."

In these circumstances, Leati's disclosures to Csopey were clearly in furtherance of the illicit association between Tome and Leati.

Csopey's testimony concerning what Leati told him about conversations between Tome and Leati is therefore admissible as "a statement by a coconspirator of a party during the course and in furtherance of the conspiracy." Rule 801(d)(2)(E), Fed.R.Evid.

2. Defendants' Objections To Bronfman's Testimony

Defendants objected to three isolated statements in Bronfman's deposition on relevancy, materiality, and competency grounds. These objections are overruled. The Bronfman deposition, in its entirety, is admissible. Defendants objections are discussed below seriatim, with the underscored portion of the deposition testimony being the portion objected to:

Bronfman Transcript pages 14-15:

Q: Other than the two matters that you mentioned to us earlier, that is to advise on currency and to invest the 10 million dollars on behalf of Seagram, was there any other business or economic relationship between Mr. Tome and Seagram or any of its affiliates that you're aware of?

A: Well, Tome is also a friend of mine, and we see each other a great deal socially and naturally we see each other socially and we talk about a lot of things in a business nature. And *I consider him sort of a European consultant to Seagram generally. It's not a formal relationship.*

Defendants object to the underscored portion of the testimony on the grounds that it is inappropriate opinion testimony by Bronfman and is inadmissible to prove that Tome was in fact a European consultant to Seagram. The relationship between Tome on the one hand and Bronfman and Seagram on the other, however, goes to the heart of this controversy. Bronfman's, and thus Seagram's, view of the employment and relationship with Tome, and the information disclosed within the parameters of that relationship, is extremely relevant and admissible to determine whether Bronfman and Seagram had an expectation that Tome would keep nonpublic information disclosed to him within the confines of the fiduciary or similar relationship confidential. *Dirks v. SEC*, 463 U.S. 646, 655 n.14, 103 S.Ct. 3255, 3262 n. 14, 77 L.Ed.2d 911 (1983). Moreover, Bronfman, as Chairman of the Board and Chief Executive Officer of Seagram, had

substantial control over the amount of confidential information disclosed to Tome. Bronfman's understanding of his (and Seagram's) relationship with Tome is therefore helpful in determining the scope of Tome's access to confidential information.

Bronfman Transcript pages 49-50

Q. In connection with this discussion, did you say in words or substance to Mr. Tome that the information you were discussing with him was confidential?

A. No. *I didn't think that was necessary.*

Q. Because?

A. Management 20 years in this business. *He ought to know the rules. I assume he does know the rules.*

Defendants object to the underscored portions of the testimony on the grounds that Bronfman cannot testify as to the state of mind of Tome, nor as to what Tome understood his relationship with Seagram and Bronfman to be, since there is no evidence in this passage that Bronfman communicated his confidentiality concerns to Tome. This argument is a spurious one for several reasons. There is direct evidence emanating from Tome that he communicated to Bronfman his understanding that the information Bronfman confided to Tome, solely for the corporate purposes of Seagram, was to be kept confidential. After this suit was filed by the SEC, naming Unknown Purchasers in Switzerland as having engaged in these illegal St. Joe transactions, Bronfman called Tome to make sure he was not involved in the St. Joe trades. Tome responded to Bronfman's inquiry by stating:

You know, I've been in this business [*i.e.*, securities] for 20 years and I know what to do and what not to do. And clearly I certainly didn't do anything.

In addition, the relationship between the management of a corporation and its financial advisors and consultants regarding prospective hostile tender offers is inherently one which implies a

duty of confidentiality. *See Dirks*, 463 U.S. at 655 n. 14, 103 S.Ct. at 3262 n. 14. Moreover, Bronfman's (and therefore Seagram's) understanding of their relationship with Tome is of course relevant because it bears on the expectation of Seagram and Bronfman that the information confided to Tome would be kept confidential. *See id.*

Bronfman Transcript page 93

Q. Why did you call Mr. Tome?

A. I called him because the S.E.C. had initiated this suit and *I was concerned that perhaps he had done something. I wanted to make doubly sure he hadn't. Because the only person I knew in Switzerland that would have any knowledge one way or another of anything that was going on, at least for me, was Mr. Tome.*

Defendants object to the underscored portion of the testimony on the grounds that it is opinion testimony for which no proper foundation has been laid and that it is irrelevant to prove Tome's knowledge of Seagram's tender offer plans. These objections are overruled. The quoted passage explains Bronfman's motive for calling Tome in Switzerland as soon as Bronfman learned that the SEC had filed suit against Unknown Purchasers who purchased St. Joe securities through BSI, a Swiss Bank. It is highly relevant that Bronfman, the person calling the shots in Seagram's search for an acquisition and the person through whom Tome wangled his way into Seagram's affairs, picked up the phone after learning of the suit to ask Tome whether he had done anything improper with the information Bronfman had confided to him. Bronfman's act of telephoning Tome speaks louder than any words could.

3. Defendants' Objections To Certain SEC Exhibits

After trial, both sides submitted additional exhibits into evidence and opposing counsel for each side objected to the other's offer. The SEC's objections to defendants' exhibits are overruled

and all exhibits offered by defendants, both at and after trial, are received in evidence and have been reviewed.

The SEC submitted certain exhibits after trial to which the defendants offered only generalized objection.⁵ One of the objections was that the exhibits (as was other information) were furnished after the Court sessions and while matters that were anticipated but had not been lodged with the Court were forthcoming. In response to the objection, the Court advised defendants' counsel that permission had been granted to supply the data, that exhibits 700, 907, 908, 909, and 913 bore on the issues or contained matter not reasonably controvertible and that "If you or Mr. Schachner have any *specific* objection to any *specific* portion of these enumerated exhibits, the Court will entertain them if received within five days of receipt of this letter." No specific objection was presented. These exhibits are received in evidence.

A further dispute arose as to the admissibility of certain trading records. Suffice it to say that the trading records of transactions so far as they refer to transactions in St. Joe call options or stock are received and those records referring to other stocks or transactions in other stocks or options are excluded. Such records of St. Joe items were known to defendants well in advance of trial, data therefrom was incorporated in the agreed findings of fact, and compilations thereof may be received appropriately in evidence under Rules 803(6), (8), (17), and (24), Fed.R.Evid. The remaining exhibits offered by the SEC post-trial are excluded.

So Ordered.

⁵ Exhibits 900, 901, 902, 903, 904, 905 and 906 were received in evidence without objection.

SECURITIES AND EXCHANGE COMMISSION, Plaintiff,

v.

Giuseppe B. TOME, Paolo Mario Leati, Lombardfin S.p.A.,
Trasatlantic Financial Co., S.A., Nayarit Investments, S.A., Finvest
Underwriters and Dealers Corp., Certain Purchasers of the Com-
mon Stock and Call Options for the Common Stock of St. Joe
Minerals Corp., and Banca Della Svizzera Italiana, Defendants.

81 Civ. 1836 (MP).

United States District Court,
S.D. New York.

July 22, 1986.

MEMORANDUM ACCOMPANYING JUDGMENT

MILTON POLLACK, Senior District Judge.

Prejudgment Interest

The Findings and Opinion in this case, filed June 3, 1986, stated that prejudgment interest on the amounts subject to disgorgement in this civil insider trading action brought by the SEC, was to be calculated at the average prime rate for the period from March 11, 1986, the day after the unlawful purchase of St. Joe securities based on inside information, through the date of the Findings and Opinion. This amount turned out to be approximately 13% per annum. On further consideration, after hearing arguments of counsel, this Court amends the prior Opinion to rule that prejudgment interest shall be included in the judgment at the rate of 9% per annum for the period from March 11, 1986, through July 22, 1986, the date of the entry of final judgment. This 9% shall be included on all of the unlawful St. Joe trades discussed in the Opinion; the main defendant, Tome, is liable for prejudgment interest both on trades in which he had a beneficial interest and, jointly and severally with his tippees,

on trades in which he tipped others to trade but in which the SEC did not demonstrate that he had a beneficial interest.

“An award of pre-judgment interest in a case involving violations of the federal securities laws rests within the equitable discretion of the district court to be exercised according to considerations of fairness.” *Chris-Craft Industries, Inc. v. Piper Aircraft Corp.*, 516 F.2d 172, 191 (2d Cir.1975) (involving Section 14(e) of the Securities Exchange Act of 1934), *rev'd on other grounds*, 430 U.S. 1, 97 S.Ct. 926, 51 L.Ed.2d 124 (1977). *Accord Blau v. Lehman*, 368 U.S. 403, 414, 82 S.Ct. 451, 457, 7 L.Ed.2d 403 (1962) (involving insider's “short swing” profits under § 16(b) of the Securities Exchange Act of 1934); *Woods v. Barnett Bank of Fort Lauderdale*, 765 F.2d 1004, 1014 (11th Cir.1985) (violation of Rule 10b-5); *Huddleston v. Herman & MacLean*, 640 F.2d 534, 560 (5th Cir.1981) (violation of Rule 10b-5), *aff'd in part, rev'd in part on other grounds*, 459 U.S. 375, 103 S.Ct. 633, 74 L.Ed.2d 548 (1983); *Elkind v. Liggett & Myers, Inc.*, 635 F.2d 156, 173 n. 30 (2d Cir.1980) (violation of Rule 10b-5); *Wessel v. Buhler*, 437 F.2d 279, 284 (9th Cir.1971) (violation of Rule 10b-5).

Tome contends that it would be inequitable (and therefore an unlawful “penalty” in a disgorgement proceeding) to compel him to pay prejudgment interest on profits from his tippers' transactions since he did not have a beneficial or discretionary interest in those transactions. He contends that he should not have to pay prejudgment interest on money that he never received and for which he is liable only derivatively or vicariously.¹ In a Rule 10b-5

¹ The Supreme Court has held that the tipper's conduct, almost invariably, is more culpable than that of the tippee. *Bateman Eichler, Hill Richards, Inc. v. Berner*, — U.S. —, 105 S.Ct. 2622, 2630-31, 86 L.Ed.2d 215 (1985). Moreover, a tipper's liability is independent, not derivative, of the tippee's. *SEC v. Tome*, 81 Civ. 1836, slip op. at 58-59 n. 40 (S.D.N.Y. June 3, 1986). But if the tippee can be held liable as well, the tipper's liability is joint and several with that of his tippee. *Bateman*, 105 S.Ct. at 2630; *Elkind*, 635 F.2d at 169. A tippee, however, *cannot* be held liable unless the tipper is also liable. *Dirks v. SEC*, 463 U.S. 646, 662, 103 S.Ct. 3255, 3265, 77 L.Ed.2d 911 (1983). Given these propositions, it is illogical to argue, as Tome does, that a tippee's liability can be *greater* than that of the tippee, *i.e.*, that, as to the tippee's trades, the tippee can be held liable for prejudgment interest but that the tipper cannot.

case, however, the Second Circuit has held that "the fact that the defendants were not unjustly enriched does not, standing alone, make it inequitable to compel them to pay interest." *Rolf v. Blyth, Eastman Dillon & Co.*, 637 F.2d 77, 87 (2d Cir.1980).

In another insider trading case, another defendant put forth the argument Tome now asserts, claiming that its liability in damages for tippee trading should be limited because it did not benefit financially from the tippees' transactions. *Elkind v. Liggett & Myers, Inc.*, 472 F.Supp. 123, 134 (S.D.N.Y.1978), *aff'd in relevant part*, 635 F.2d 156 (2d Cir.1980).² In rejecting this argument and imposing liability on the defendant both for damages and for prejudgment interest based on its tippees' transactions, the district court noted that the defendant "acted in order to obtain other benefits[.]" *i.e.*, to foster goodwill between it and the financial analysts it tipped. *Id.* The Second Circuit affirmed the district court's finding of liability against the defendant based on its tippees' trades, specifically noting that "[t]he district court acted well within its discretion in awarding prejudgment interest . . . " on those transactions. *Elkind*, 635 F.2d at 169, 173 n. 80.

An award of prejudgment interest "is, in the first instance, compensatory[.]" but this "compensatory principle must be tempered by an assessment of the equities." *Norte & Co. v. Huffines*, 416 F.2d 1189, 1191 (2d Cir.1969), *cert. denied sub nom.*, *Muscat v. Norte & Co.*, 397 U.S. 989, 90 S.Ct. 1121, 25 L.Ed.2d 396 (1970). In this case, Tome willfully violated the securities laws and thereafter attempted, through lies and deceit, to cover-up his role in the illegal activity; he has remained outside the United States to avoid prosecution on related criminal charges. In short, the equities do not weigh in his favor. *See id.* ("personal wrongdoings" of defendant should be considered in evaluating whether an

² In this case, however, there is evidence that Tome did benefit financially from the tippee transactions. Tome was to be paid \$200,000 for the tip to Leati, a tip that Tome *intended* Leati use for the benefit of Leati's firm's, Lombardfin S.p.A.'s customers. As to Tome's other tippees, he had a brokerage relationship with them and certainly expected to benefit financially through increased business from these clients in other transactions.

award of prejudgment interest is in accord with "fundamental fairness"); *Wessel*, 437 F.2d at 284 (remanding to district court for determination of prejudgment interest in a Rule 10b-5 case because of defendant's "flagrant use of false statements.").

In setting an appropriate prejudgment interest rate, this Court notes that the average prime rate during this period of time has been almost 13% per annum. Approximating what the return on a relatively safe investment during this time would have been, this Court sets the prejudgment interest rate at 9% per annum. See *Western Federal Corp. v. Davis*, 553 F.Supp. 818, 821 (D.Ariz.1982) (for a violation of Section 12 of the Securities Act of 1933, using a prejudgment interest rate of 14.25%, which was the consumer money market rate, as a benchmark, and adjusting downwards depending on the degree to which plaintiffs lost the use of their money), *aff'd sub nom.*, *Western Federal Corp. v. Erickson*, 739 F.2d 1439 (9th Cir. 1984).

So Ordered.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

-----X
SECURITIES and EXCHANGE COMMISSION,

Plaintiff,

-against-

GIUSEPPE B. TOME, PAOLO MARIO LEATI, LOMBARD-
FIN S.p.A., TRASATLANTIC FINANCIAL CO., S.A., NAYARIT
INVESTMENTS, S.A., FINVEST UNDERWRITERS AND
DEALERS CORP., CERTAIN PURCHASERS OF THE COM-
MON STOCK AND CALL OPTIONS FOR THE COMMON
STOCK OF ST. JOE MINERALS CORP., AND BANCA DELLA
SVIZZERA ITALIANA,

Defendants.
-----X

81 Civ. 1836 (MP)

JUDGMENT

This action came on for trial before the Court, Honorable Mil-
ton Pollack, Senior District Judge presiding, and the issues hav-
ing been duly tried and a decision having been duly rendered, it is

I

ORDERED, ADJUDGED AND DECREED;

A. That the defendant Giuseppe B. Tome ("Tome") is found
liable for, and plaintiff shall recover from said defendant who shall
disgorge the sum of \$3,476,706.00 together with prejudgment in-
terest of 9% per annum for the period from March 11, 1981 to
July 22, 1986, the date of entry of this judgment, which amounts
to \$1,677,677.30; for a total of \$5,154,383.30.

B. That the defendant Trasatlantic Financial Co., S.A., ("Trasatlantic") is jointly and severally liable with the defendant Tome for, and plaintiff shall recover from said defendant who shall disgorge profits in the amount of \$450,769.40 together with prejudgment interest of 9% per annum for the period from March 11, 1981 to July 22, 1986, the date of entry of this judgment, which amounts to \$217,517.82 for a total of \$668,287.22.

C. That the defendant Nayarit Investments, S.A. ("Nayarit") is jointly and severally liable with the defendant Tome for, and plaintiff shall recover from said defendant who shall disgorge profits in the amount of \$723,331.00 together with prejudgment interest of 9% per annum for the period from March 11, 1981 to July 22, 1986, the date of entry of this judgment, which amounts to \$349,032.22; for a total of \$1,072,363.20.

D. That the defendant Finvest Underwriters and Dealers Corp. ("Finvest Panama") is jointly and severally liable with the defendant Tome for, and plaintiff shall recover from said defendant who shall disgorge profits in the amount of \$273,277.00 together with prejudgment interest of 9% per annum for the period from March 11, 1981 to July 22, 1986, the date of entry of this judgment, which amounts to \$131,869.25; for a total of \$405,146.25; and Irving Trust Company of New York shall also sell and turn over to the registry of this Court the proceeds of 1,200 shares of Fluor Corporation stock in its possession subject to this Court's orders, plus dividends which have accrued since March 11, 1981. The said proceeds and dividends turned over shall be credited on account of the liability of Tome and Finvest Panama hereunder.

E. That the defendants Lombardfin S.p.A. ("Lombardfin") and Paolo Mario Leati ("Leati") are jointly and severally liable with the defendant Tome for, and plaintiff shall recover from said defendant who shall disgorge profits in the amount of \$1,345,925.00 together with prejudgment interest of 9% per annum for the period from March 11, 1981 to July 22, 1986, the date of entry of this judgment, which amounts to \$649,473.32; for a total of \$1,995,368.30.

F. Any amount paid on account of any defendant other than Tome shall be credited toward the liability of Tome under subdivision A hereof.

G. BSI is liable for and shall pay into the Registry of this Court the deposit of \$2,000,000 in its possession frozen pursuant to the Court's prior orders at the Irving Trust Company of New York to cover the liabilities of Trasatlantic, Nayarit and Finvest Panama, plus any interest which directly or indirectly has been credited during said deposit to the credit of BSI or any of the said defendants. BSI's maximum liability hereunder shall not exceed the aggregate liability of Trasatlantic, Nayarit and Finvest Panama on account of trading activities through BSI.

H. That this action as against Defendants Certain Purchasers of the Common Stock and Call Options for the Common Stock of St. Joe Minerals Corporation ("the Unknown Purchasers", i.e., other than Trasatlantic, Nayarit, Finvest Panama) be and hereby is dismissed without prejudice.

I. Let execution issue accordingly.

II

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that the defendants, Tome, Nayarit, Trasatlantic, Finvest Panama, Leati, Lombardin, their agents, servants, employees, attorneys-in-fact and those persons in active concert or participation with them and each of them, be and hereby are permanently enjoined and restrained from, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange:

- (1) employing any device, scheme, or artifice to defraud;
- (2) making any untrue statement of material fact or omitting to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or

- (3) engaging in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security, in violation of Sections 10(b) and 14(e) of the Exchange Act, 15 U.S.C. § 78j(b) and 78n(e), to the extent their prohibitions are coextensive, and Rules 10b-5 and 14e-3, 17 C.F.R. § 240.10b-5 and 240.14e-3, promulgated pursuant to the Exchange Act, to the extent that the prohibitions of the Rules are coextensive, by, among other things:

- (1) misappropriating, converting or obtaining by other illegal acts, in breach of a fiduciary duty, material nonpublic information concerning, *inter alia*, publicly traded companies or actual or proposed business combinations involving a public company; and
- (2) purchasing or selling securities of such companies or causing such securities to be purchased or sold, unless within a reasonable time prior to such purchase or sale, such information and its source are publicly disclosed; or
- (3) conveying or causing the conveyance of such information to persons, knowing, or having reason to know, such persons will purchase or sell or cause the purchase or sale of securities of such companies.

III

IT IS FURTHER ORDERED AND ADJUDGED that all of the foregoing amounts be paid in the following manner:

- (1) the amounts to be paid shall be paid into the registry of this Court by certified check(s) drawn to the order of "Clerk, United States District Court, S.D.N.Y.", whereupon the Clerk of this Court, or the financial deputy clerk, is hereby directed to deposit check(s) in an interest-bearing account, as a time deposit, at the Manufacturers Hanover Trust Company, Branch #35, 277 Broadway, New York,

New York (the "Depository") so as to maximize the return on minimum risk investments, i.e. such sums may be invested in the higher yielding of United States Treasury Bills or Certificates of Deposit;

- (2) the account shall be held by the Depository as a time deposit for an initial period of 90 days; thereafter it should be held for successive periods of 90 days, subject to any further orders of this Court;
- (3) interest earned on the account shall be credited to the account and shall thereafter be treated in the same manner as principal;
- (4) distribution of sums paid by the defendants pursuant to this Order shall be effected according to a plan for disgorgement and administration to be submitted by the Commission and approved by this Court and added to the foot of this decree.

IV

IT IS FURTHER ORDERED that this Court shall retain jurisdiction over this matter for all purposes.

s/ Milton Pollack

SENIOR UNITED STATES
DISTRICT JUDGE

Dated: New York, New York
July 22, 1986

JUDGMENT ENTERED:

s/ Raymond F. Burghardt

CLERK